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105TH CONGRESS
2d Session

SENATE

REPORT
105–336

THE FINANCIAL SERVICES ACT OF 1998

REPORT

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

TO ACCOMPANY

H.R. 10

together with

ADDITIONAL VIEWS

SEPTEMBER 18, 1998.—Ordered to be printed

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105TH CONGRESS, 2d Session — SENATE — REPORT 105–336

THE FINANCIAL SERVICES ACT OF 1998

SEPTEMBER 18, 1998.—Ordered to be printed

Mr. D'AMATO, from the Committee on Banking, Housing, and Urban Affairs, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany H.R. 10]

The Committee on Banking, Housing, and Urban Affairs, to which was referred the bill (H.R. 10), having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

INTRODUCTION

On September 11, 1998, the Senate Committee on Banking, Housing, and Urban Affairs (the "Committee") marked up and ordered to be reported H.R. 10, the "Financial Services Act of 1998," to enhance competition in the financial services industry by providing a prudential framework for the affiliation of banks, securities firms, and other financial service providers, and for other purposes. The Committee reports the bill favorably with amendments, and recommends that the bill do pass.

HISTORY OF LEGISLATION

On May 14, 1998, H.R. 10, the "Financial Services Act of 1998," was referred to the Committee after passage in the House of Representatives. The Committee held four days of hearings on this landmark legislation to modernize the financial system and the laws governing financial intermediaries. At the first hearing on Wednesday, June 17, Secretary of the Treasury Robert Rubin and Federal Reserve Chairman Alan Greenspan testified. On Thursday, June 18, the Committee received testimony from James F. Higgins, President and Chief Operating Officer, Morgan Stanley, Dean Witter and Company, representing the Securities Industry Association, Washington, D.C.; Matthew P. Fink, President, the Investment Company Institute, Washington, D.C.; William A. Fitzgerald, Chairman and CEO, Commercial Federal Bank, representing America's Community Bankers, Omaha, NE.; John Heimann, Chairman, Global Financial Institutions, Merrill Lynch & Company, representing the Financial Services Council, Washington, D.C.; John H. Biggs, Chairman of the Board and CEO, Teachers Insurance and Annuity Association, representing American Council of Life Insurance, American Insurance Association, National Association of Mutual Insurance Companies, National Association of Independent Insurers, Alliance of American Insurers, Washington, D.C.; Robert A. Miller, Chairman, the National Association of Life Underwriters Financial Institutions Task Force, also representing the Independent Insurance Agents of America, the Council of Insurance Agents and Brokers, the National Association of Professional Insurance Agents, Washington, D.C.; William T. McConnell, President, American Bankers Association, Washington, D.C.; Richard M. Kovacevich, Chairman and CEO, Norwest Corporation, representing the Bankers Roundtable, Washington, D.C.; and William McQuillan, Chairman, President, and CEO, the City National Bank, President of the Independent Bankers Association, Greeley, NE.

On the third day of hearings, Wednesday, June 24, the following witnesses and organizations presented testimony to the Committee: Ralph Nader, Consumer Advocate, Washington, D.C.; Mary Griffin, Insurance Counsel, on behalf of Consumers Union and the Consumer Federation of America, Washington, D.C.; Edmund Mierzwinski, Consumer Program Director, U.S. Public Interest Research Group, Washington, D.C.; Allen Fishbein, General Counsel, Center for Community Change, Washington, D.C.; and John Taylor, President and CEO, National Community Reinvestment Coalition.

On Thursday, June 25, at the final hearing, the following Federal regulatory agencies and organizations representing State regulators appeared and testified: Julie L. Williams, Acting Comptroller of the Currency; Ellen Seidman, Director, Office of Thrift Supervision; Arthur Levitt, Chairman, Securities and Exchange Commission; Donna Tanoue, Chairman, Federal Deposit Insurance Corporation; Timothy R. McTaggart, Bank Commissioner, Delaware Department of Banking, on behalf of the Conference of State Bank Supervisors, Washington, D.C.; George Nichols, III, Commissioner of Insurance, State of Kentucky and Chairman of NAIC Special Committee on Banks and Insurance, on behalf of the National Association of Insurance Commissioners, Washington, D.C.; Denise Voight Crawford, Texas Securities Commissioner and President of the North American Securities Administrators Association, Washington, D.C.; and James Pledger, Commissioner, Texas Savings and Loan Department, on behalf of the American Council of State Savings Supervisors, Austin, Texas.

On September 11, the Committee met in Executive Session to mark-up H.R. 10. The Committee considered and adopted, without objection, a Manager's Amendment that was offered by Chairman

D'Amato and the Ranking Member, Senator Sarbanes, that incorporated amendments submitted by other Committee Members that were agreed to on a bipartisan basis.

During the mark-up, the Committee considered several other amendments. Senator Allard offered an amendment which was adopted on a 10 to 8 vote to delete the low cost banking account provisions of the House-passed bill. On behalf of himself and Senator Dodd, Senator Sarbanes offered an amendment to direct the Federal bank and securities regulators to issue rules to require financial institutions, before selling or sharing customers' confidential financial information, such as account balances or other transaction or experience data, to give customers prior notice, to give customers an opportunity to verify the accuracy of information and to obtain customers' consent to such disclosures. The amendment failed on a 10 to 8 vote. Chairman D'Amato and Senator Bryan then offered, and the Committee adopted on a voice vote, an amendment to protect the confidentiality of consumer financial information from so-called "information brokers" attempting to obtain personal information under false pretenses.

The Committee then voted 16–2 to report H.R. 10 to the Senate for consideration. Senators Gramm and Shelby voted against the motion to report the bill from the Committee.

BACKGROUND

For over a decade, the Committee has been concerned that the statutory framework governing financial services has become outdated. Many of the statutes addressing financial services, dating from the Great Depression or even earlier, are not well adapted to the changes taking place in the financial services industry. In particular, developments in technology, globalization of financial services, and changes in the capital markets have rendered the laws governing financial services unsuitable and outdated in many respects. In 1988 and in 1991, the Committee reported bills that would have modernized the regulation of financial services.[1] In reporting H.R. 10 to the Senate, the Committee resumes its bipartisan effort to provide a regulatory framework suitable for financial services in the twenty-first century.

NEED FOR THE LEGISLATION

The Committee believes that overhaul of our financial services regulatory framework is necessary in order to maintain the competitiveness of our financial institutions, to preserve the safety and soundness of our financial system, and to ensure that American consumers enjoy the best and broadest access to financial services possible with adequate consumer protections. It is important that the statutes regulating financial services promote these goals because of the crucial role that financial services play in the American economy. Not only does the financial services industry account for 7.5 percent of our nation's gross domestic product and employ

[1] In 1988 the Committee reported S. 1886, the Financial Modernization Act of 1988. While the Senate passed this legislation, the full House took no action. In 1991 the Committee reported S. 543, the Comprehensive Deposit Insurance Reform and Taxpayer Protection Act of 1991. While portions of this bill were enacted as the "FDIC Improvement Act of 1991", the provisions restructuring the financial services industry were not enacted into law.

5 percent of our workforce, it is vital to the growth of the rest of the economy by serving as a channel for capital and credit. The financial services industry provides opportunities for savers, investors, borrowers, and businesses to realize their goals. It allows for the transfer of various kinds of risk to those most able to bear those risks. The pace of economic growth in this country depends in large part on the ability of the financial services industry to function efficiently.

The financial services industry is currently constrained by statutes that impose hurdles or outright prohibitions on the affiliation of banks on the one hand and securities firms and insurance companies on the other. These restrictions, many of which were enacted after the bank failures of the Great Depression, were intended to protect the financial system by insulating commercial banking from other forms of risk. Over time, these restrictions have hampered the ability of financial institutions to diversify their products. This inability to diversify actually increases risks to the financial system. By limiting competition, the outdated statutes also reduce incentives to develop new and more efficient products and services. This deprives consumers of the benefits of the marketplace.

Federal Deposit Insurance Corporation (FDIC) Chairman Donna Tanoue indicated that the current system, which divides the various sectors of the financial services industry, should be updated:

> The rapidly evolving financial marketplace is subject to the oversight of a regulatory structure that was formed when financial products, services, and organizations were well-differentiated. Today, many banking, securities, and insurance products overlap in purpose, effect, and appearance. The recent announcements of mergers between very large banking organizations and between banking organizations and other financial entities highlight the extensive changes taking place. To ensure that the oversight system for the financial industry is adequate for the task of maintaining stability while allowing orderly evolution, the system's statutory foundations require modernization.[2]

As the various sectors of financial services converge, providers of financial services are seeking to serve customers better by combining those sectors in one organization. Testifying for the Financial Services Council, John Heimann, a former Comptroller of the Currency, described the blurring of the divisions between the financial services sectors:

> Consumer needs have prompted the development of financial services that were rare or unknown not long ago—services like mutual funds, money market accounts, credit cards, mortgages, individual retirement accounts, home equity loans, stored value cards, and a variety of products geared to the business owner. Many of these new products are the result of an increasing level of competition by financial services providers across industry lines, providing alternatives to services once available only from a single

[2] Tanoue Testimony at 2.

> source. Thus, money market mutual funds were developed by the securities industry to provide an investment opportunity for funds that consumers were holding in bank accounts. Banks offer loan syndications and private placements of securities to business clients as an alternative to services offered by securities firms. Life insurance companies developed single premium annuities to compete with bank certificates of deposit.[3]

In addition, as the number of nations participating in the global capital markets increases, providers of financial services are seeking greater economies of scale. John Heimann described the pressure that U.S. firms are experiencing:

> Despite the consolidation occurring in the U.S., most of the largest financial services companies are today still headquartered outside this country. If our industry is to remain competitive around the world—especially as financial reform comes to the European Union—we must take steps to maintain the global preeminence of U.S.-based financial corporations and of our nation's financial markets.[4]

As banks, insurance companies, and securities firms enter one another's markets, regulation of financial services has become increasingly arbitrary. Witnesses identified numerous examples of this phenomenon to the Committee. Under current regulatory interpretation, national banks may sell insurance nationwide so long as such sales are based in a place of less than 5,000 people. Sales of insurance products may be subject to significantly different regulation depending on whether those sales are made by a bank or an insurance agent. Similarly, sales of securities may be regulated differently depending on whether they take place through a bank or a securities broker.

In many cases, existing statutes create impediments and inefficiencies for the affiliations occurring in the marketplace. Regulators and courts have on occasion fashioned paths around these impediments, but such actions are no substitute for the establishment of fundamental policy by Congress. As Federal Reserve Chairman Alan Greenspan testified:

> Without Congressional action, changes will occur through exploitation of loopholes and marginal interpretations of the law that courts feel obliged to sanction. This type of response to market forces lead to inefficiencies, expansion of the Federal safety net, potentially increased risk exposure to the Federal Deposit insurance funds, and a system that will undermine the competitiveness and innovative edge of major segments of the financial services industry.[5]

Creating a new statutory framework for the financial services industry should translate into greater safety and soundness for the

[3] Heimann Testimony at 9–10.
[4] Heimann Testimony at 4.
[5] Greenspan Testimony at 2.

financial system, increased efficiency for financial services providers, and more choices and lower costs for consumers.

PURPOSE AND SCOPE OF THE LEGISLATION

H.R.10, as reported by the Committee, employs the same general approach as the House-passed version of H.R.10 and as the bills reported by the Committee in 1988 and 1991. First, the bill repeals the provisions of the Glass-Steagall Act that restrict the ability of banks and securities underwriters to affiliate with one another. Second, within the framework of the Bank Holding Company Act, the bill creates a new category of "financial holding company." The financial holding company vehicle allows for a broader range of financial services to be affiliated, including commercial banking, insurance underwriting and merchant banking as defined in the legislation. The bill maintains the current separation of banking and commerce in our financial system. It also contains provisions intended to provide appropriate regulation of bank sales of insurance.

Permissible affiliations

The core of the legislation is the creation of a new type of bank holding company called a "financial holding company." Banks, securities firms, and insurance companies will be able to affiliate with one another through the financial holding company model. Financial holding companies will be allowed to engage in activities that are "financial in nature." This is a broader standard than the "closely related to banking" standard that currently delineates the permissible activities of bank holding companies.

The Committee believes that allowing broader affiliations within the financial holding company should place no segment of the financial services industry at a disadvantage. Banks, insurance companies, and securities firms should have equal opportunities to affiliate with one another. At the same time, financial holding companies should not compete unfairly with banks, insurance companies, and securities firms that choose to remain unaffiliated.

Broader affiliations within the holding company structure will present new challenges for safety and soundness regulation of financial institutions. To meet these challenges, the bill provides for regulation of financial holding companies by the Federal Reserve Board (the "Board"). The bill also provides for functional regulation of activities; that is, similar activities should be subject to the same regulatory scheme.

Organizational structure

The Committee carefully analyzed whether the holding company or the operating subsidiary approach is the appropriate organizational structure for new activities conducted by an insured bank. Some have characterized this debate as solely one of jurisdiction between the Board and the Treasury. The Committee disagrees. This is a fundamental issue which must be handled carefully in the context of the significant reforms in activities that we are considering.

Congress must be careful to provide sufficient safeguards for our new financial framework. The Committee does not want to see a repeat of the savings and loan crisis where the taxpayer had to bail out federally insured institutions that assumed excessive risks and operated without effective management, internal controls, and supervision. Congress must ensure that the Federal safety net is not extended in any way. The deposit insurance funds must be adequately insulated from paying the losses of firms which are affiliated with insured banks. The Committee believes that the holding company structure best achieves this purpose. Under this approach, if an affiliate fails, the losses will not affect the bank.

The Committee took into consideration Federal Reserve Chairman Greenspan's views on this topic. Many distinguished former regulators share his views. In a recent editorial, former Federal Reserve Chairman Paul Volcker recently wrote:

> The commercial bank must be a separate organization, insulated legally from its sister entities providing financial services. Moreover, that arrangement is more easily compatible with continued "functional" supervision of the component parts * * *.[6]

Finally, the Committee has previously endorsed the holding company framework. In 1991, the Committee approved S. 543, which repealed the Glass-Steagall Act and allowed banks to affiliate with securities firms using the holding company structure to ensure safety and soundness, a level competitive playing field, and protection of the taxpayer. H.R. 10 uses the same holding company framework as S. 543, but expands the range of permissible financial affiliations to include insurance underwriting and merchant banking.

Permissible activities

Not only does the bill allow for broader affiliations between banks and other providers of financial services, but the bill also expands the activities in which banks may engage. Section 121 of the bill allows national bank subsidiaries to engage in any type of financial agency activity. With respect to agency activities other than the sale of insurance products, the bill would prohibit States from preventing or restricting bank activities in these areas.

Insurance activities

The Committee recognizes that insurance sales and other insurance activities present a unique set of problems and challenges. Insurance, unlike either banking or securities activities, is wholly governed by the regulatory apparatus established in each State—an arrangement confirmed by the McCarran-Ferguson Act of 1945.[7]

Although banks have previously been allowed to sell insurance in places with a population of 5,000 people or less (Section 92 of the National Bank Act), there is no Federal insurance law analogous to either the Federal securities laws (such as the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, or the Investment Advisors Act of 1940) or the Federal banking laws (such as the National Bank Act, the Bank Holding Company Act or the Consumer Credit Protection Act).

[6] Volcker, Paul. "Boost for Banking". Washington Post. September 10, 1998.
[7] The Act of March 9, 1945.

As a result, the relationship between the banking industry and State insurance regulators has been uneasy at best, and uncertainty over regulation of bank insurance sales has often been exacerbated by certain Federal bank regulators that have often been clumsy or heavy-handed in their attempts to establish regulatory parameters for insurance sales. Moreover, there has been ample evidence that some State statutes—either on their face or in their application—have made it virtually impossible for a bank to sell insurance products effectively.

In order to strike a careful balance that recognizes the need and desirability of continued State regulation of insurance activities as well as the necessity to remove unfair impediments placed on bank activities in this area, the Committee made several changes to Section 104 of the bill.

The bill permits banks to sell any type of insurance product from any location, in contrast to the increasingly artificial construction of the "place of 5,000" requirement. However, the bill clearly establishes that it is the State insurance regulator—not Federal bank regulators—that is the appropriate functional regulator of a bank's (for the purposes of discussing Section 104, the term "bank" shall mean "an insured depository institution or a wholesale financial institution or any subsidiary or affiliate thereof") sales of insurance products, provided that such regulation meets certain criteria.

The bill holds, as a general rule, that States may not "prevent or significantly interfere" with the insurance sales, solicitations, or cross-marketing of "an insured depository institution or a wholesale financial institution or any subsidiary or affiliate thereof". However, the Committee recognizes that a bank's sales of products that are not insured by the FDIC or that may be required to be obtained in connection with a loan or other traditional bank product present certain circumstances under which it may be necessary for the protection of consumers for a State to treat a bank's sale of insurance differently than insurance sales by entities unaffiliated with a bank. To address this important distinction and to protect consumers, the Committee established a safe harbor of thirteen different areas in which a State can treat a bank's sales of insurance differently than the sales by unaffiliated entities. State laws which fall under the safe harbor are exempt from challenge under the various remedies provided elsewhere in this section.

As noted above, the Committee is also mindful of the history of State insurance statutes, regulations, orders, and other actions which have made it virtually impossible for a bank to sell insurance. As a result, the Committee has made remedies available to protect banks from prohibitive, discriminatory, or interfering regulation. First, as a general rule, States may not "prevent or significantly interfere" with a bank's insurance sales activities. Second, for State laws that are enacted prior to September 3, 1998, and which fall outside the bill's safe harbor, the bill does not limit in any way the application of the Supreme Court's decision in *Barnett Bank* v. *Nelson*.[8] State laws outside the safe harbor could be challenged under that decision. Moreover, the Office of Comptroller of the Currency (OCC) would retain all deference currently accorded

[8] 116 S. Ct. 1103 (1996).

it in applying *Barnett* to the laws enacted prior to September 3, 1998. Third, State laws enacted on or after September 3, 1998, which do not fall into the bill's safe harbor would be subject to a non-discrimination test made up of four distinct criteria. This test would prevent States from enacting laws that are discriminatory on their face, which create a significant disparate impact on banks as compared to other entities selling insurance, which effectively prevent a bank's sale of insurance, or which generally conflict with the intent of this bill. Furthermore, the bill does not limit in any way the application of the Supreme Court's decision in *Barnett* and those laws outside the safe harbor could be challenged under that decision. However, for laws which are subject to the non-discrimination test (e.g., which are enacted on or after September 3, 1998), the OCC would be accorded no unequal deference, as spelled out in Section 307(e) of the bill.

Securities activities

H.R. 10 expands bank activities in the securities area as well. National banks are given authority to underwrite municipal revenue bonds, in addition to their existing authority to underwrite general obligation bonds.

The Committee made a number of changes to Subtitle A of Title II, relating to the functional regulation of broker-dealers. First, the Committee adopted several revisions that the North American Securities Administrators Association suggested. These changes reflect the new division between the Commission and the States of regulatory responsibility for investment advisors that was adopted as part of the National Securities Markets Improvement Act of 1996.[9]

The other changes that were adopted pertain to the treatment of: banking products that are also "securities" for the purposes of the Federal securities laws and certain traditional banking activities that involve securities transactions. Currently, banks are exempted from the definition of "broker" and "dealer" in the Securities and Exchange Act of 1934 (the "1934 Act"), and are therefore not required to register as broker-dealers with the Commission. Registration as a broker-dealer was deemed unnecessary when the 1934 Act was enacted because of the Glass-Steagall Act. As a general rule, banks were prohibited from "securities" activities; in light of this general prohibition, and the existing bank regulatory framework, there was no need to regulate banks as broker-dealers.[10]

In recent years, the bank regulators have permitted banks and bank holding companies to expand their securities activities. H.R. 10 accommodates this trend within a functional regulatory framework. The repeal of Glass-Steagall's anti-affiliation rules and the blanket exemption for banks from broker-dealer registration raises the issue whether, and under what circumstances, such products and activities should be "pushed out" of (i.e., moved out of) a bank and into a registered broker-dealer affiliate.

[9] P.L. 104–290 (approved October 11, 1996).

[10] *See, e.g.,* Hearings on H.R. 10 Before the Senate Committee on Banking, Housing and Urban Affairs, June 25, 1998 (Testimony of Arthur Levitt, Chairman of Securities and Exchange Commission, Concerning H.R. 10, note 5 and accompanying text).

The Committee believes that the House-passed version of H.R. 10 required too many activities to be "pushed-out" of the bank and placed too many restrictions on the conduct of traditional banking services. Clearly, to the extent that banks want to engage in full-service brokerage activities, such activities should be "pushed-out" to an SEC-registered affiliate or subsidiary. Nevertheless, banks have historically provided largely ministerial securities services, frequently through their trust departments. Banks are uniquely qualified to provide these services and have done so without any problems for years. Banks provided trust services under the strict mandates of State trust and fiduciary law without problems long before Glass-Steagall was enacted; there is no compelling policy reason for changing Federal regulation of bank trust departments, solely because Glass-Steagall is being modified. Under IRS regulations, banks must offer self-directed Individual Retirement Accounts ("IRAs") in either a trustee or custodial capacity. Services rendered as a trustee do not require registration as a broker-dealer to the extent that these services fall within the trust exemption. The Committee believes that bank custodial, safekeeping, and clearing activities with respect to IRAs do not need to be pushed-out into an SEC-registered broker-dealer.

The Committee also revised the bank transfer agent provisions. The House-passed provisions would have disrupted services for employee benefit plans, dividend reinvestment plans, and issuer plans. Currently, such service plans can offer direct execution services to participants through transfer agents. By removing the intermediaries from the execution process, these plans provide cost-savings for their participants. The transfer agents receive a payment which is calculated based on transaction volume (typically, a set number of basis points of the volume).

The House-passed version of H.R. 10 would have precluded the offering of such services for transaction-based fees. This would have made such services prohibitively expensive. Since transfer agent activities are regulated, and the transaction-based fees are for ministerial services which provide significant cost-savings for shareholders, the Committee decided to eliminate this restriction.[11]

The Committee also amended the provisions of the House bill that set limitations on other traditional bank activities that may or do involve transactions in products that qualify as securities: private placements and derivative transactions. The Committee believes that, to the extent that these transactions are conducted with sophisticated and experienced investors, there is no compelling reason to "push-out" these activities (which have been supervised by banking regulators). This approach is consistent with the treatment of such transactions under Federal securities laws.

The Committee believes that the House-passed version of H.R. 10 established a one-sided process for determining how to regulate future "hybrid" products (i.e., products that have both banking and securities characteristics). Section 206 of the bill was amended to give both the Board and the Securities and Exchange Commission a role in determining whether such hybrid products must be

[11] Hearings on H.R. 10 Before the Senate Committee on Banking, Housing and Urban Affairs, June 25, 1998 (Submission prepared by ABA Securities Association, p.12 (referred to in testimony of William T. McConnell, on behalf of the American Bankers Association)).

pushed-out to a registered broker-dealer. The Committee believes these changes will allow banks to develop new products cheaply and efficiently, while giving due consideration to the dual goals of safety-and-soundness and investor protection. The Committee also removed Section 251 of the bill. This section contained unnecessary and redundant disclosure requirements.

The bill creates a new Section 6 of the Bank Holding Company Act. Section 6(H) recognizes the essential role that principal investing, or merchant banking, plays in modern finance. A financial holding company or its non-bank affiliate (collectively, the "FHC") whether directly, indirectly, or through a fund, may make investments in any amount in, or otherwise acquire control of, a portfolio company, or its board of directors, subject to conditions designed to maintain the separation between banking and commerce. The ownership interests must be acquired for appreciation and ultimate resale or other disposition. Such disposition can be subject to a variety of factors, including overall market conditions, the condition and results of operation of the portfolio company's business, and its duties to co-investors and advisory clients. The Committee recognizes that certain investments may be held for a period of time in order to realize their potential value. Another condition imposed by Section 6(H) is that the FHC may not actively manage or operate the portfolio company, except insofar as necessary to achieve the investment objectives. The Committee recognizes that employees of the FHC may have dealings with the management of a portfolio company. The word "actively" was used to distinguish occasional participation in management from continuous participation; the reference to "day to day management" was used to suggest that participation is not limited to the company's board of directors. The language makes clear that it may be necessary for the investor to intervene in daily management in order to protect its investment.

The Committee believes that compliance with the requirements of Section 6(H) can be ascertained either by periodic reports from, or by examination of, the holding company or affiliate making the investment. No examination of the portfolio company is necessary other than in the case in which reports or examinations are necessary to assure compliance with restrictions governing transactions involving depository institutions and portfolios companies.

Furthermore, the Committee intends Section 6(H) to permit investment banking firms to continue to conduct their principal investing in substantially the same manner as at present. An FHC should not be placed at a competitive disadvantage with firms unaffiliated with any depository institution. The Board shall not require, even informally, any pre-clearance of principal investments and not impose arbitrary or unduly restrictive limitations on the holding period for such investments. Moreover, the Board should challenge the management or operation of the portfolio company or the exercise of discretion regarding the duration of an investment only if clearly inconsistent with the purposes of this section. Finally, the Committee intends that the Board be the sole entity with legal standing to allege that an FHC is in violation of Section 6(H) with respect to a particular investment.

Functional regulation

The bill generally adheres to the principle of functional regulation, which holds that similar activities should be regulated by the same regulator. Different regulators have expertise at supervising different activities. It is inefficient and impractical to expect a regulator to have or to develop expertise in regulating all aspects of financial services. Accordingly, the bill is intended to ensure that banking activities are regulated by bank regulators, securities activities are regulated by securities regulators, and insurance activities are regulated by insurance regulators. The bill establishes procedures for determining whether future products should be underwritten within a bank, subject to banking regulation, or by an insurance company subject to insurance regulation. Similarly, the bill contains procedures for determining whether new products should be subject to banking regulation or securities regulation.

The bill repeals the blanket exemption banks currently enjoy from the definitions of "broker" and "dealer" under the Federal securities laws. Instead, the bill delineates specific securities activities that banks may conduct without registering with the Commission. These provisions are intended to allow banks to continue to engage in securities activities that have already been permitted by, and are subject to, regulation by bank regulators. Trust activities, custody, safekeeping, derivatives dealing, private placement of securities, and underwriting of asset-backed securities that fall within the bill's provisions may remain in banks. Securities activities that do not fall within the bill's provisions must take place in broker-dealers regulated by the Commission.

Treasury role in determining "financial in nature"

The Committee believes that the Treasury Department's views regarding what activities are "financial in nature" are highly relevant. Accordingly, the Committee has revised the bill to create an explicit role for the Treasury Department in the Board's review process.

The Board must coordinate and consult with the Treasury Department in making its determinations regarding financial activities. The Board may not determine that an activity is financial if the Treasury believes that it is not financial or incidental to a financial activity. The Treasury may also recommend that an activity be deemed to be financial, and the Board must determine within thirty days whether to initiate a public rulemaking regarding the proposal.

Holding company regulation

The bill seeks to provide regulation of FHCs that is sufficient to protect the safety and soundness of the financial system and the integrity of the Federal deposit insurance funds without imposing unnecessary regulatory burdens. While functional regulators are supervising various holding company subsidiaries, the Committee believes there is a need for oversight of the organization as a whole as well as subsidiaries not subject to functional regulation. The need for holding company regulation was stressed by witnesses before the Committee as well. For example, William McQuillan, President of City National Bank of Greeley, N.E., testified, "[t]he

IBAA strongly supports the establishment of an umbrella regulator for diversified financial services firms and feels the only Federal regulator equipped for this job is the Federal Reserve."[12]

Accordingly, the bill gives the Board authority to adopt consolidated capital requirements for financial holding companies. The Board also has authority to examine the holding company and, under certain circumstances, any holding company subsidiary that poses a material risk to an affiliated bank.

The Committee does not intend for holding company regulation to override functional regulation of holding company subsidiaries. For functionally regulated subsidiaries, the Board is required, to the greatest extent possible, to rely on reports required by and examinations conducted by the functional regulator. Thus, the Board must generally defer to regulation by the State insurance commissioners, the State and Federal banking agencies, the Commission, the State securities commissioners, and appropriate self regulatory organizations. The Board may not require that an insurance company or securities firm provide financial support to a troubled bank affiliate if the functional regulator determines this would have a materially adverse effect on the financial condition of the insurance company or securities firm.

Too-big-to-fail

The Committee felt strongly that language should be added to the House-passed bill to address the "too-big-to-fail" concerns. Accordingly, the bill amends the Federal Deposit Insurance Act to prevent the use of Federal deposit insurance funds to assist affiliates or subsidiaries of insured financial institutions. The intent of this provision is to ensure that the FDIC's deposit insurance funds not be used to protect uninsured affiliates of financial conglomerates.

Prior notice for large non-banking acquisitions

The Committee believes that the Board should have prior notice of and authority to disapprove of a large financial merger because of its potential impact on the financial system. The bill requires FHCs and wholesale financial holding companies seeking to acquire companies with assets in excess of $40 billion (or companies that would become FHCs as a result of such acquisition), to give 60 days prior notice to the Board. The Board is given the authority to disapprove the proposed acquisitions. The bill enumerates the factors that the Board shall consider in making this determination, and the agencies with which the Board shall confer with as a part of this process.

Community Reinvestment Act (CRA)

The Committee preserved the provisions of H.R. 10 with respect to the Community Reinvestment Act (CRA) with the following exceptions:

The bill eliminates the specific remedy of divestiture, where the Board would have been authorized to require financial holding companies whose bank subsidiaries do not maintain a satisfactory

[12] McQuillan Testimony at 2.

CRA rating to divest control of any depository institution subsidiary. In addition, National banks that do not maintain a satisfactory CRA rating would not be required to divest subsidiaries.

The bill applies CRA only to Wholesale Financial Institutions (WFI's) that are affiliated with insured banks. The bill also deletes the application of CRA to foreign banks, as well as the CRA study by Treasury.

Unitary thrift holding companies

The Committee adopted changes to Title IV of the House-passed version of H.R. 10. These changes reflect a careful balancing of the diverse views held by Committee members.

Some Committee members strongly hold the view that mixing banking and commerce poses serious risks to the safety and soundness of the financial system, distorts credit decisions by banks, and leads to undue concentrations of economic power. Since H.R. 10 generally maintains the separation of banking and commerce, they felt strongly that the unitary holding company loophole to the separation of banking and commerce should be closed.

However, other Committee members feel strongly that the unitary thrift structure has posed no undue supervisory risk and, in fact, represents a model for financial reform. These members point to the long history of the unitary structure and the lack of evidence that the structure has presented any safety and soundness threat. In fact, these members believe that commercial affiliations authority enhances the pool of capital and managerial talent available to unitary thrifts, as evidenced by the acquisition of some thrifts during the savings and loan crisis.

To balance these concerns, the Committee modified the provisions in the House bill concerning unitary thrift holding companies, as recommended by the Board's Chairman Alan Greenspan. Section 401 of H.R. 10 as reported by the Committee prohibits any company that engages, directly or through a subsidiary, in commercial activities from directly or indirectly acquiring control of a savings association after September 3, 1998. It also prohibits any savings and loan holding company from engaging, directly or through a subsidiary, in commercial activities.

Existing unitary savings and loan holding companies are exempted from these restrictions. These prohibitions do not apply to a unitary savings and loan holding company in existence on September 3, 1998, or that was formed pursuant to an application pending before the Office of Thrift Supervision (OTS) on or before that date, provided that the company continues to meet the requirements to be a unitary savings and loan holding company under 12 U.S.C. 1467(a)(c)(3) and to control at least one of the savings associations that the company controlled (or had applied to control) as of September 3, 1998, or the successor to such a savings association (a "grandfathered unitary savings and loan holding company").

The purpose of this provision of the bill is to prohibit any company directly or indirectly engaged in commercial activities (other than a grandfathered unitary savings and loan holding company) from acquiring control of a savings association after September 3, 1998, by or through any means including through any forward or reverse merger, consolidation, or other type of business combination. Section 401 authorizes the OTS to issue such regulations, interpretations, and orders as may be necessary to prevent evasions of this prohibition, and the Committee expects the OTS to take all actions necessary to carry out the purpose of this section, which is to prohibit firms engaged in commercial activities from acquiring control of any savings association. In particular, the Committee expects that the OTS will use this authority to prohibit transactions that, although structured to appear as the acquisition of a commercial firm by a grandfathered savings and loan holding company, would in substance result in a commercial company or its shareholders acquiring control of a savings and loan holding company or any of its savings association subsidiaries.

In making such determinations or taking other actions under Section 401, the OTS should use the definition of "control" set forth in section 10 of the Home Owners Loan Act.

Consumer protections

The Committee recognizes the importance of protecting consumers who will now be able to purchase a broader range of financial products from affiliated providers of financial services on the premises of or through banks. The wider variety of financial products available at a bank raises potential customer confusion about the insured status, risks, the issuer and the seller of the new products. The Committee is concerned about past instances in which depositors have purchased unsuitable investment products without understanding their nature, and wants to take reasonable steps to prevent misunderstanding and confusion when bank customers receive unsolicited sales presentations or see advertisements for securities and insurance products for purchase through the bank.

The bill requires sales to take place in an area separate from the deposit-taking that is clearly marked, so that retail customers can distinguish whether a bank, a securities broker or insurance agent is offering the product. Salespersons would be required to inform potential customers about whether the products are insured or carry risks with conspicuous and readily understandable disclosures before sales occur, and would be prohibited from misrepresenting the products' uninsured nature. The bill requires sales personnel to be appropriately licensed. Unlicensed employees, such as tellers, would be allowed to receive a nominal, one-time, fixed-dollar fee for referring a customer to the stock or insurance broker, provided such fee's payment is not conditioned on whether the customer executes a transaction.

The bill requires the Federal bank regulators, in consultation with State insurance authorities, to issue regulations that are consistent with the requirements of the Act that apply to the retail sale of insurance products by or through banks. The Commission would administer the amended provisions of the Securities Exchange Act of 1934 affecting the retail sales of securities through networking arrangements on or off bank premises.

Federal home loan banks

The Committee adopted a substitute for the House-passed provisions addressing the Federal Home Loan Bank (FHLB) System. The last major reform of the FHLB system took place in the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA). Prior to FIRREA, only thrifts could be members of the FHLB system and access the system's advances. In 1989, Congress permitted commercial banks to gain access to the system. The provisions in the bill addressing the FHLB system are intended to recognize the changes in membership and regulatory structure put in place by FIRREA.

There are four major provisions in the bill affecting the FHLB system. The first changes the membership of thrifts from mandatory to voluntary. The system provides enough benefits to its members to ensure that it can sustain itself on the membership of those who wish to join. Second, the bill gives small banks greater access to advances by expanding the types of assets they may pledge as collateral. Third, the Resolution Funding Corporation (REFCorp) obligation was changed from a fixed dollar figure to a percentage of the system's current net earnings. Lastly, many of the day-to-day management functions of the individual banks were taken away from the Federal Housing Finance Board (FHFB), the system's safety and soundness regulator. Many of the day-to-day functions of the FHLBanks currently require approval from the FHFB. These approval requirements largely date to an earlier period when the FHLBanks were regulated by the Federal Home Loan Bank Board. Several studies, including one by the General Accounting Office (GAO), have suggested that the FHFB is too involved in day-to-day management decisions of the FHLBanks.

Foreign banks

At the recommendation of the Board, the Committee adopted several provisions to provide parity between foreign banks and their domestic counterparts.

Capital standards for foreign banks

The House bill required the Board to establish and apply comparable capital standards for foreign banks that wish to be treated as financial holding companies. The Committee added a provision to clarify the Board's current authority to require foreign banks to meet other requirements for FHCs. For example, the "well managed" criteria literally applies only to insured depository institutions, e.g., the U.S. bank and thrift subsidiaries. Accordingly, the Committee adopted an amendment to give the Board explicit authority with regard to other operating standards applicable to FHCs.

Restriction on transactions with affiliates

The House bill authorizes the Board to impose additional restrictions on transactions or relationships only between U.S. banks and thrifts and their nonbank affiliates. The Committee amended these provisions to include authority to impose restrictions on transactions and relationships between the foreign bank and its U.S. nonbank affiliates.

Amendments to international banking act

Congress amended the International Bank Act (IBA) in 1991, after the Bank of Credit and Commerce International (BCCI) affair, to require that a foreign bank could not establish a representative office without obtaining the prior approval of the Board. In keeping with the common understanding of representative offices, a subsidiary of a foreign bank was excluded from the IBA definition of a representative office. The Committee has become aware that some foreign banks are seeking to avoid the prior approval requirement of the IBA by establishing separate subsidiaries or using existing nonbank subsidiaries to act as representative offices. Although the subsidiary is separately incorporated, it carries out the same representative function as if it were a traditional representative office of the foreign bank. A number of States do not distinguish between representative offices that are direct offices of the foreign bank and those that are subsidiaries. Accordingly, the bill would eliminate this loophole by striking the subsidiary exclusion from the definition of representative offices.

In addition, the bill clarifies the Board's authority to examine a U.S. affiliate of a foreign bank with a representative office in order to determine the compliance of the representative office with requirements of U.S. law. Presently, if a foreign bank has only a representative office and no other banking office in the United States, the Board may examine only the representative office. The Board cannot currently examine or seek information from U.S. affiliates of such foreign bank. This limitation could become a problem if there were serious questions raised about the nature or legality of relationships or transactions between the representative office and its U.S. affiliates. To illustrate such a problem, it must be recalled that BCCI illegally used its representative offices to engage in deposit-taking and money laundering in the United States.

In addition, the bill permits U.S. Attorney's Offices to seek a court order to provide financial institution regulatory agencies with access to grand jury material, thereby giving State regulatory agencies parity with Federal regulatory agencies.

Privacy

The Committee adopted the "Financial Information Privacy Act" to address the significant threat to financial privacy posed by an emerging industry of so-called "information brokers," some of whom use deception and false pretenses to collect personal financial information for their clients. The legislation authorizes civil and criminal penalties for a person who uses fraud or deception to obtain, or attempt to obtain, customer information from a financial institution. This legislation amends the Consumer Credit Protection Act by adding a new title consisting of eight sections.

Community Banks

Small independent banks are confronting unprecedented challenges as a result of growing competition from all financial service providers, the accelerating pace of technological change and the innovation it promotes, changing demographic patterns, and shifting consumer attitudes towards managing their personal finances. The Committee has attempted in this and other legislation within its jurisdiction to recognize the importance of community-oriented banks to our economy and the local markets they serve.

Because the Committee wants to make every effort to preserve the role of community banks, this bill includes a Sense of the Committee Resolution underscoring the importance of changes to the Internal Revenue Code to reduce the tax burden on community banks and recommending to the Senate that such changes should be adopted by Congress in conjunction with financial modernization legislation. This Committee Resolution is not intended to intrude on the responsibilities of the Senate or any of its committees; only to underscore this Committee's ongoing effort to strengthen community banks.

Technical corrections and miscellaneous provisions

The Committee also adopted the following technical changes to the H.R.10.

The bill repeals section 3(f) of the Bank Holding Company Act to conform the regulation of savings bank life insurance with the regulations governing all other financial institutions in a bank holding company structure.

The bill amends the Federal Deposit Insurance Act to allow a holding corporation (formerly a GSE) that was privatized by Federal legislation to enter into an affiliation arrangement with an insured depository institution provided that the Secretary of the Treasury approves the affiliation and determines that the successful wind-down of the GSE will not be affected and that the GSE will otherwise be separate from the arrangement. The Secretary of the Treasury is authorized to impose any conditions on the affiliation that the Secretary deems appropriate.

The bill deletes provisions concerning the redomestication of mutual insurers.

The bill deletes erroneous references and provide other technical corrections.

SECTION-BY-SECTION ANALYSIS

Title I—Facilitating Affiliation Among Securities Firms, Insurance Companies, and Depository Institutions

SUBTITLE A—AFFILIATIONS

Section 101. Glass-Steagall reformed

Section 101 repeals Sections 20 and 32 of the Glass-Steagall Act, allowing affiliations and interlocking employment among banks and securities firms.

Section 102. Activity restrictions applicable to bank holding companies which are not financial holding companies

Section 102 applies activity restrictions to bank holding companies that are not financial holding companies, and makes conforming changes to the Bank Holding Company Act Amendments of 1970 and the Bank Service Company Act.

Section 103. Financial holding companies

Section 103 defines a new structure, called a "financial holding company" (FHC), under which banks may affiliate with securities and insurance firms. A holding company qualifies as a FHC if all of its insured depository subsidiaries are well capitalized and well managed, and maintain Community Reinvestment Act (CRA) ratings of at least "satisfactory."

Certain FHCs may engage in a broad range of activities that are "financial in nature" or "incidental to financial activities," including:

Lending and other traditional bank activities;

Insurance underwriting and agency activities;

Providing financial, investment, or economic advisory services;

Issuing instruments representing interests in pools of assets that a bank may own directly;

Securities underwriting and dealing, and mutual fund distribution;

Merchant banking;

Any activity that the Federal Reserve Board (the "Board") has deemed "closely related to banking" under the Bank Holding Company Act;

Any activity that the Board has already approved for U.S. banks operating abroad; and

Any other activity the Board may approve as "financial" or "incidental" to a financial activity.

The Board will determine by regulation or order which activities are financial in nature or incidental to financial activities. In determining whether activities are financial in nature or incidental to financial activities, the Board must take into account expected changes in markets or technology, and international competition.

The Board must coordinate and consult with the Treasury Department in making its determinations regarding financial activities. The Board may not determine that an activity is financial if the Treasury believes that it is not financial or incidental to a financial activity. The Treasury may also recommend that an activity be deemed financial, and the Board must determine within 30 days whether to initiate a public rulemaking regarding the proposal.

FHCs and wholesale financial holding companies (WHFCs) may merge with other financial companies without prior notice to or approval from the Board, unless the acquired company has assets exceeding $40 billion. If the acquired company's assets exceed $40 billion, the FHC proposing the acquisition must provide the Board with notice at least 60 days prior to the proposed acquisition. The Board may disapprove the acquisition within that time period, which the Board may extend by an additional 60 days. The section details factors which the Board must consider in making a determination about a proposed acquisition.

Section 103 permits financial holding companies to engage in a broad range of financial activities and activities that are incidental to financial activities, and grants the Board new authority to define those activities. In determining whether an activity is financial in nature or incidental to one or more financial activities, the Committee intends that the Board take into account a number of factors. Those factors include the purposes of the Financial Services Act and the Bank Holding Company Act, changes that have occurred or are reasonably expected in the marketplace in which financial holding companies compete or in the technology for delivering financial services, whether the activity in necessary and appropriate to allow a financial holding company and its affiliates to compete effectively with any company seeking to provide financial services in the United States, and any available or emerging technological means for providing financial services to customers or allowing customers to use financial services.

This authority includes authority to allow activities that are reasonably connected to one or more financial activities. For example, the Board has, under the existing closely related to banking test, permitted bank holding companies to engage in activities, such as processing any type of data or providing general management consulting services, that are incidental to permissible nonbanking activities and are relatively small in scale. The Board has also allowed bank holding companies to market excess capacities that have been developed or acquired in the course of conducting permissible activities, in order that bank holding companies may make and plan for the most cost effective acquisition of technological and other facilities. This authority provides the Board with some flexibility to accommodate the affiliation of depository institutions with insurance companies, securities firms, and other financial services providers while continuing to be attentive not to allow the general mixing of banking and commerce in contravention of the purposes of this Act.

Section 104. Operation of State law

Section 104(a), in general, pre-empts a state's ability to prevent or restrict affiliations between financial entities, except that a State insurance regulator may continue to require notice and specified information about potential purchasers of insurance companies in order to ensure that all mandated capital requirements are met and maintained, and to place an insurance company into receivership or conservatorship.

Section 104(b)(1), in general, pre-empts a State's ability to prevent or restrict the sales activities authorized under this Act of an insured depository institution with the exception of insurance sales and other insurance activities.

Section 104(b)(2) governs State regulation of insurance sales so that States may not prevent or significantly interfere with the insurance sales of an insured depository institution, except that a State may enact restrictions contained in the thirteen points of the safe harbor listed in section 104(b)(2)(B).

With respect to State laws on insurance sales enacted prior to September 3, 1998, but which fall outside the provisions of 104(b)(2)(B), those laws are subject to the Supreme Court's *Barnett* decision and, in connection with those laws, the Comptroller of the Currency retains deference.

With respect to State laws on insurance sales enacted on or after September 3, 1998, but which fall outside the provisions of 104(b)(2)(B), those laws are subject to the anti-discrimination test of contained in section 104(c) and can also be subject to the Supreme Court's *Barnett* decision. However, the provisions of Section 307(e) will apply, under which the Comptroller of the Currency will not enjoy unequal deference.

Section 104(b)(3) ensures that insurance companies affiliated with insured depository institutions continue to be governed by the domiciliary State as envisioned under the McCarran-Ferguson Act, provided that the laws are consistent with the provisions of Section 104(c).

Section 104(c) creates a standard for State regulation of insurance that prevents a State, on or after September 3, 1998, from discriminating against insurance sales or activities by insured depository institutions.

Section 105. Mutual bank holding companies authorized

Section 105 authorizes mutual bank holding companies, which are to be regulated in a manner comparable to other bank holding companies.

Section 106. Prohibition on deposit production offices

Section 106 places references to the Financial Services Act of 1998 in the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994.

Section 107. Clarification of branch closure requirements

Section 107 clarifies bank branch closure requirements under Section 42 of the Federal Deposit Insurance Act.

Section 108. Amendments relating to limited purpose banks

Section 108(a) amends Section 4(f) of the Bank Holding Company Act. Section 4(f) provides that certain companies that control banks are not treated as bank holding companies. These are companies that control banks that, prior to the Competitive Equality Banking Act of 1987, either made commercial loans or accepted insured deposits but did not do both. Under Section 4(f)(2)(A)(ii), such companies may not acquire control of more than 5 percent of the shares or assets of an additional bank or savings association, other than certain enumerated exceptions. Section 108(a) amends Section 4(f)(2)(A)(ii) to allow these companies to acquire consumer loan assets derived from or incidental to activities in which credit card banks and industrial loan companies are permitted to engage, without losing their exemption from treatment as bank holding companies under the Bank Holding Company Act.

Section 108(b) amends Section 2(c)(2)(H) of the Bank Holding Company Act. Section 2(c)(2)(H) exempts industrial loan companies from the definition of "bank" for purposes of the Bank Holding Company Act. Under Section 2(c)(2)(H), the exemption is conditioned on an industrial loan company's not permitting an overdraft on behalf of an affiliate, or incurring an overdraft on behalf of an affiliate at its account at a Federal Reserve bank, unless such overdraft is the result of an inadvertent computer or accounting error. Section 108(b) amends Section 2(c)(2)(H) to allow industrial loan companies to incur the same overdrafts on behalf of affiliates as are permitted for banks described in Section 4(f)(1) of the Bank Holding Company Act (banks that, prior to the enactment of the Competitive Equality Banking Act of 1987, either made commercial loans or accepted insured deposits but did not do both).

Section 109. Reports on ongoing FTC study of consumer privacy issues

Section 109 requires the FTC to submit interim reports on its study of consumer privacy issues.

Section 110. General Accounting Office study of economic impact on community banks and other small financial institutions

Section 110 requires the General Accounting Office (GAO) to study the projected impact of this Act on financial institutions with assets of $100 million or less.

SUBTITLE B—STREAMLINING SUPERVISION OF FINANCIAL HOLDING COMPANIES

Section 111. Streamlining financial holding company supervision

Section 111 provides that the Board may require any bank holding company or subsidiary thereof to submit reports informing the Board of its financial condition, financial systems and statutory compliance. The Board is directed to use existing examination reports prepared by other regulators, publicly reported information and reports filed with other agencies to the fullest extent possible.

The Board is authorized to examine each bank holding company and its subsidiaries. However, it may examine nondepository institution holding company subsidiaries only if the Board has reasonable cause to believe that the subsidiary is engaged in activities that pose a material risk to the depository institution or is not in compliance with certain statutory and regulatory restrictions. The Board is directed to use to the fullest extent possible examinations made by appropriate Federal and State regulators.

If a bank holding company is not "significantly engaged" in nonbanking activities (e.g., a shell holding company), the bill would authorize the Board to designate the appropriate bank regulatory agency of the lead depository institution subsidiary as the appropriate Federal banking agency for the bank holding company.

The Board is required to defer:

To the Securities and Exchange Commission (the "Commission") to interpret all Federal securities laws applicable to the activities, conduct, and operations of registered brokers, dealers, investment advisers, and investment companies;

To the relevant State securities authorities to interpret State securities laws relating to the activities, conduct and operations of registered brokers, dealers, and investment advisers; and

To the relevant State insurance regulators to interpret insurance laws relating to the activities, conduct and operations of insurance companies and insurance agents.

The Board is not authorized to prescribe capital requirements for any nondepository subsidiary of a financial holding company. In developing, establishing, and assessing holding company capital or capital adequacy rules, guidelines, standards, or requirements, the Board also has been prohibited from taking into account the activities, operations, or investments of an affiliated investment company, unless the investment company is a bank holding company or a bank holding company owns more than 25 percent of the shares of the investment company (other than certain small investment companies). The Committee adopted this measure because investment companies are specially regulated entities that must meet diversification, liquidity, and other requirements specifically suited to their role as investment vehicles. Consequently, the Committee believed that it was important to ensure that the Board not indirectly regulate these entities through the imposition of capital requirements at the holding company level, except in the very limited circumstances noted above.

Section 112. Elimination of application requirement for financial holding companies

Section 112 amends Section 5(a) of the Bank Holding Company Act of 1956 to provide that a declaration filed in accordance with Section 6(b)(1)(E) will satisfy the requirements of Section 5(a) with regard to the registration of a bank holding company, but not a requirement to file an application pursuant to Section 3. This eliminates duplicative filing requirements.

Section 113. Authority of State Insurance Regulator and Securities and Exchange Commission

Section 113 amends Section 5 of the Bank Holding Company Act of 1956 to prohibit the Board from requiring a broker-dealer or insurance company that is a bank holding company to infuse funds into an insured depository subsidiary if the holding company's functional regulator, the Commission or State insurance regulator, determines in writing that "such action would have a material adverse effect on the financial condition of the insurance company or the broker or dealer, as the case may be." If the Commission or State insurance regulator makes such a determination, the Board can order the holding company to divest the insured depository institution.

Section 114. Prudential safeguards

Section 114 authorizes the Board to adopt rules governing the relationships between bank holding companies' depository institution subsidiaries and other subsidiaries if the Board finds that such rules:

Are consistent with the public interest and Federal law, and would avoid significant risks to the safety and soundness of depository institutions;

Enhance the financial stability of bank holding companies;

Avoid conflicts of interests or other abuses;

Enhance the privacy of customers of depository institutions; or

Promote the principles of national treatment and equality of competitive opportunity for nonbank affiliates of domestic bank holding companies and nonbank affiliates owned or controlled by foreign banks operating in the U.S.

Section 115. Examination of investment companies

Section 115 authorizes the Commission to be the sole Federal agency with authority to inspect and examine any registered investment company that is not a bank holding company.

Section 116. Limitation on rulemaking, prudential, supervisory and enforcement authority of the Board

Section 116 adds a new Section 10A to the Bank Holding Company Act. Section 10A is intended to protect regulated subsidiaries, which already are subject to extensive regulation at the hands of their functional regulators, from additional and duplicative regulation by the Board. Section 10A prohibits the Board from becoming involved in or interfering with the regular, day-to-day business and operations of regulated subsidiaries. Section 10A also prohibits the Board from taking any action under specified statutes where the purpose or effect of doing so would be to override a determination that an activity is financial in nature and thereby exclude regulated subsidiaries from a line of business that is financial in nature or prevent regulated subsidiaries from offering a product or service that is financial in nature. None of the above would prevent the Board from taking action in an individual case where the manner in which an activity is conducted renders action necessary to prevent or redress an unsafe or unsound practice or breach of fiduciary duty by a regulated subsidiary that poses a material risk to the financial safety, soundness or stability of an affiliated depository institution or to the domestic or international payment system.

The Committee intends the term "material risk" to mean a risk of serious harm to the financial safety, soundness or stability of the particular depository institution at issue or to the payment system. In considering whether it is not reasonably possible to effectively protect against risk through action directed at an affiliated depository institution or depository institutions generally, the Board must consider the full scope of any statutory authority it and the other federal banking agencies may have over any type of depository institution, including national banks and state nonmember banks, under any statute which the Board and the other federal banking agencies are authorized to administer. In this regard, the Committee expects the Board, if necessary and possible, to request other federal banking agencies to exercise their authority in order to protect against any feared risk, and the Committee expects the other agencies to coordinate with and accommodate requests for action by the Board.

Section 117. Interagency consultation

Section 117 states the Committee's intent that the Board as the umbrella regulator, the appropriate Federal banking regulator, and the State insurance regulator as the functional regulator of insurance activities, should consult with each other and share examination reports and other information. It provides that upon the request of a State insurance regulator, the Board may provide any information regarding the financial condition, risk management policies, and operations of any financial holding company that controls an insurance company regulated by that State insurance regulator, and vice versa. It further provides that upon the request of a State insurance regulator, the appropriate Federal banking agency may provide information about any transaction or relationship between a depository institution and affiliated insurance company regulated by that State insurance regulator, and vice versa. In addition, the appropriate Federal banking regulator is required to consult with the appropriate State insurance regulator before making determinations between a depository institution, wholesale financial institution, or financial holding company with an insurance company.

Section 118. Equivalent regulation and supervision

Section 118 provides that the provisions of both Section 5(c) of the Bank Holding Company Act of 1956 and Section 10A of the Bank Holding Company Act of 1956 also limit any authority that the Director of the Office of Thrift Supervision (OTS) and Comptroller of the Currency (OCC) have under any statute to require reports, make examinations, impose capital requirements, or take any other action with respect to bank holding companies and their nonbank subsidiaries. Section 5(c) of the Bank Holding Company Act of 1956 limits the authority of the Board to require reports of, make examinations of, and to impose capital requirements on bank holding companies and their nonbank subsidiaries. Section 10A of the Bank Holding Company Act of 1956 which limits any Board authority to take action with respect to bank holding companies and their nonbank subsidiaries. The OTS and the OCC are subject to the same standards and requirements as are applicable to the Board under these provisions.

This section ensures that these agencies will not be able to assume and duplicate the function of being the general supervisor over regulated subsidiaries which has been appropriately left to their functional regulators. The Committee recognizes that, under the concept of functional regulation, the extent of the authority of these agencies to take actions under any statute against, or with respect to, regulated subsidiaries should not be any greater than that of the Board under Sections 111 and 116.

Section 119. Prohibition on FDIC assistance to affiliates and subsidiaries

Section 119 amends Section 11(a)(4)(B) of the Federal Deposit Insurance Act generally to prohibit the use of the Bank Insurance Fund and the Savings Association Insurance Fund to benefit any shareholder, subsidiary or nondepository affiliate.

SUBTITLE C—SUBSIDIARIES OF NATIONAL BANKS

Section 121. Permissible activities for subsidiaries of National banks

Section 121 provides that National bank subsidiaries can engage only in those activities permissible for National banks to engage in directly, those otherwise expressly authorized by statute, when or acting as an agent in activities that are financial in nature or incidental to financial activities under the Bank Holding Company Act; provided that the bank is well-capitalized, well-managed, rated "satisfactory" for CRA, and approved for the activity by the OCC. Non-bank activities, such as underwriting insurance, must be conducted in holding company affiliates, and not through subsidiaries of the bank. There is a limited exclusion from the community needs requirements for newly acquired depository institutions.

Section 122. Misrepresentations regarding depository institution liability for obligations of affiliates

Section 122 makes it a crime for bank personnel to fraudulently represent that the bank will be liable for any obligation of a bank affiliate or subsidiary.

Section 123. Repeal of stock loan limit in Federal Reserve Act

Section 123 repeals Section 11(m) of the Federal Reserve Act, relating to the Board's ability to fix the percentage of individual bank capital and surplus which may be represented by loans secured by stock or bond collateral made by member banks.

SUBTITLE D—WHOLESALE FINANCIAL HOLDING COMPANIES; WHOLESALE FINANCIAL INSTITUTIONS

Section 131. Wholesale financial holding companies established

Section 131 establishes Wholesale Financial Holding Companies (WFHC), defining a WFHC as a FHC that is predominantly financial, controls one or more Wholesale Financial Institutions (WFIs), and is not affiliated with an insured bank or savings association. WFHCs are subject to supervision by the Board, which may adopt capital adequacy rules for them. Commercial activities of WFHCs are grandfathered, but may not be expanded through merger or consolidation.

Section 132. Authorization to release reports

Section 132 authorizes the release of certain reports under the Federal Reserve Act, and includes the Commodity Futures Trading Commission under the definitions of the Right to Financial Privacy Act.

Section 133. Conforming amendments

Section 133 makes conforming amendments to the Bank Holding Company Act and the Federal Deposit Insurance Act.

Section 136. Wholesale financial institutions

Section 136 establishes National Wholesale Financial Institutions, which are chartered and regulated by the Comptroller of the Currency, and State Wholesale Financial Institutions which are chartered and regulated by the States. Wholesale Financial Institutions (WFIs) generally may not accept deposits of less than $100,000. Neither National nor State WFIs may have deposit insurance. This section also provides for the termination of deposit insurance under the Federal Deposit Insurance Act so that institutions may become WFIs.

Capital requirements for all WFIs must be established by the Board, which may also impose limitations on transactions with affiliates, set special clearing balance requirements, and take other actions to protect the payments system and the discount window. The Board may also exempt WFIs from regulations applying to member banks in order to enhance safety and soundness.

State WFIs have all of the powers and privileges of National banks, and thus of National WFIs. This includes branching rights and the preemption of State laws.

WFIs are subject to prompt corrective action by the Board. All WFIs must be well capitalized and managed, and those failing these standards must take corrective action within prescribed time periods, or face divestiture.

Subsection 136(a) subjects WFIs which are affiliated with insured depository institutions or own insured branches to CRA. This provision was included to ensure that insured financial institutions could not circumvent compliance with the H.R. 10 by transferring assets and/or deposits to affiliated WFIs.

Section 136(e) is intended to parallel the National Bank Receivership Act, which provides that the FDIC shall be appointed receiver only for insured depository institutions.

SUBTITLE E—PRESERVATION OF FTC AUTHORITY

Section 141. Amendment to the Bank Holding Company Act of 1956 to modify notification and post-approval waiting period for Section 3 transactions

Section 141 sets forth a statutory requirement that the Board immediately notify the Federal Trade Commission (FTC) about transactions by a bank holding company to merge with or acquire another bank holding company if the transaction involves the acquisition of nonbank assets.

Section 142. Interagency data sharing

Section 142 provides that Federal banking regulators share with the Attorney General and the FTC any information that the antitrust agencies deem necessary for antitrust review of appropriate transactions.

Section 143. Clarification of status of subsidiaries and affiliates

Section 143 provides that financial holding companies proposing to acquire a nonbank company engaged in financial activities must provide the antitrust agencies with prior notice of the transaction under the Hart-Scott-Rodino Act. It also clarifies that any person affiliated with a depository institution that is not itself a depository institution shall not be deemed a "bank" or "savings association" for purposes of the Federal Trade Commission Act or other law enforced by the FTC. The jurisdiction of the FTC over transactions involving the non-bank affiliates and subsidiaries of banks and savings associations under the FTC Act is affirmed by stating that such entities will not be treated as banks or savings associations.

Section 144. Annual GAO report

Section 144 requires the Comptroller General of the U.S. to annually report to Congress on market concentration in the financial services industry and its impact on consumers. The annual report is to focus on affiliations and acquisitions involving depository institutions, depository institution holding companies, securities firms, and insurance companies.

SUBTITLE F—APPLYING THE PRINCIPLES OF NATIONAL TREATMENT AND EQUALITY OF COMPETITIVE OPPORTUNITY TO FOREIGN BANKS AND FOREIGN FINANCIAL INSTITUTIONS

Section 151. Applying the principles of national treatment and equality of competitive opportunity to foreign banks that are financial holding companies

Section 151 amends Section 8(c) of the International Banking Act of 1978 (IBA) by adding a new paragraph (3) to permit termination of the financial grandfathering authority granted by the IBA and other statutes to foreign banks to engage in certain financial companies. The bill provides that foreign banks should no longer be entitled to grandfathered rights after the bank has filed a declaration under section 6(b)(1)(E) of the BHCA or receives a Board determination under Section 10(d)(1) of the BHCA.

Section 152. Applying the principles of national treatment and equality of competitive opportunity to foreign banks and foreign financial institutions that are wholesale financial institutions

Section 152 amends Section 8A of the Federal Deposit Insurance Act by adding a new subsection (i) which allows an insured branch of a foreign bank to terminate voluntarily its deposit insurance under the same conditions and extent as insured State and National banks.

Section 153. Representative offices

Section 153 would require prior approval by the Board for the establishment of representative offices by a foreign bank.

SUBTITLE G—FEDERAL HOME LOAN BANK SYSTEM MODERNIZATION

Section 161. Short title

Section 161 designates this subtitle as the "Federal Home Loan Bank System Modernization Act of 1998".

Section 162. Definitions

Section 162 provides technical changes to definitions within the Federal Home Loan Bank Act ("FHLBA"). It also creates a new class of "community financial institutions" with assets less than $500 million.

Section 163. Savings association membership

Section 163 makes Federal Home Loan Bank ("FHLBank") membership voluntary for savings and loan associations. Under current law, membership is mandatory.

Section 164. Advances to members; collateral

Section 164 expands the types of assets which can be pledged as collateral for advances for certain institutions. Currently, only mortgage loans, mortgage-backed securities, FHLBank deposits, and certain other real estate assets may be used as collateral for advances. Many smaller banks are unable to hold sufficient mortgage loans to pledge as collateral. The bill would permit banks with assets of $500 million or less, to pledge small business, agriculture, rural development, and community development loans as collateral, and use the advances to fund these four types of loans. The Federal Housing Finance Board (FHFB) would also be allowed to review, and if necessary for safety and soundness, increase certain collateral standards.

Section 165. Eligibility criteria

Section 165 waives the ten percent residential mortgage asset test for FDIC-insured institutions with assets of $500 million dollars or less. All institutions are currently required to have ten percent of their total assets in residential mortgage loans in order to become members of the system.

Section 166. Management of banks

Section 166 transfers from the FHFB to the individual FHLBanks authority over a number of operational areas, including director and employee compensation, terms and conditions for advances, interest rates on advances, dividends, and forms for advance applications. The section also clarifies other powers and duties of the FHFB with regard to enforcement.

Section 167. Resolution Funding Corporation

Section 167 changes the current annual $300 million funding formula for the Resolution Funding Corporation obligations of the FHLBanks to an percentage of annual net earnings.

SUBTITLE H—DIRECT ACTIVITIES OF BANKS

Section 181. Authority of national banks to underwrite certain municipal bonds

Section 181 amends 12 U.S.C. 24(7) to expand the scope of securities activities permissible for a national bank to include municipal revenue bonds, limited obligation bonds, and other obligations that satisfy the requirements of Section 142(b)(1) of the Internal Revenue Code issued by a State or political subdivision thereof.

SUBTITLE I—DEPOSIT INSURANCE FUNDS

Section 186. Study of safety and soundness of funds

Section 186 directs the Federal Deposit Insurance Corporation to study the following aspects of the Savings Association Insurance Fund and Bank Insurance Fund: their safety and soundness and adequacy of reserves, in light of the size of newly merged institutions and affiliations with other financial institutions; their geographic concentration levels; and their required plans for possible merger of the funds.

SUBTITLE J—EFFECTIVE DATE OF TITLE

Section 191. Effective date

Section 191 provides that Title I becomes effective 270 days after enactment of the Act.

Title II—Functional Regulation

SUBTITLE A—BROKERS AND DEALERS

Section 201. Definition of broker

Section 201 amends the Securities and Exchange Act of 1934 (1934 Act) definition of "broker" to narrow the blanket exemption for banks. A "broker" is defined as "any person engaged in the business of effecting transactions in securities for the account of others". The bill exempts a bank from classification as a "broker" only to the extent that the bank engages in activities that are enumerated in this section.

Section 202. Definition of dealer

Section 202 amends the 1934 Act's blanket exemption for banks from the definition of "dealer". A "dealer" is defined as "any person engaged in the business of buying or selling securities for such person's own account through a broker or otherwise". The bill exempts a bank from classification as a "dealer" only to the extent that the bank engages in: transactions for investment purposes for accounts where the bank acts as a trustee or fiduciary; transactions in commercial paper, bank acceptances, commercial bills, qualified Canadian government obligations, and Brady bonds; the issuance or sale of asset backed securities to qualified investors; transactions in "traditional banking products"; or buying or selling derivative instruments to qualified investors.

Section 203. Registration for sales of private securities offerings

Section 203 creates a new limited qualification category of National Association of Securities Dealers, Inc. (NASD) registration for bank employees engaged in private securities offerings.

Section 204. Sales practices and complaint procedures

Section 204 directs Federal banking agencies to establish, within six months of the bill's enactment, joint regulations, similar to the NASD Rules of Fair Practice, governing the securities sales practices of insured depository institutions and their affiliates. The appropriate Federal banking agencies are directed to develop joint procedures and facilities for handling customer complaints, and for making referrals to the Commission. These required rules must be developed in consultation with the Commission.

Section 205. Information sharing

Section 205 requires Federal banking agencies, in consultation with the Commission, to establish record-keeping requirements for banks relying on the bank exceptions to "broker" or "dealer" classification. These records must be made available to the Commission upon request.

Section 206. Definition and treatment of banking products

Section 206 defines "traditional banking product," for the purposes of the bank broker-dealer exemptions. The definition includes: deposit accounts; deposit instruments issued by a bank; bankers acceptances; letters of credit or loans issued by a bank;

credit card debt accounts; loan participations sold to qualified investors; certain non-security derivative instruments; and any new product not currently regulated as a security that the Board, after consultation with the Commission, determines to be a new banking product.

With respect to new products, the Commission may object to the Board's determination, and may, within sixty days, appeal to the United States Court of Appeals for the District of Columbia Circuit. The court's consideration must affirm and enforce, or set aside, the regulation based upon whether the subject product or instrument is best regulated under Federal banking laws or Federal securities laws.

Section 207. Derivative instrument and qualified investor defined

Section 207 defines "derivative instrument". This definition excludes any derivatives that are included within the definition of "traditional banking product". Section 207 also defines "qualified investor" to include: any registered investment company; bank; savings and loan association; broker; dealer; insurance company; business development company; licensed small business investment company; State sponsored employee benefit plan or employee benefit plan under ERISA (other than an IRA); certain trusts; any market intermediary; any foreign bank or any foreign government; any corporation, company or individual who owns and invests at least $10 million; any government or political subdivision who owns and invests at least $50 million; and any multinational or supra-national entity; or any other person that the Commission determines to be a qualified investor.

Section 208. Government securities defined

Section 208 amends the 1934 Act definition of "government securities" to include qualified Canadian government obligations for the purposes of Section 15C (which governs government securities brokers) as applied to a bank.

Section 209. Effective date

Section 209 provides that the subtitle shall take effect 270 days after enactment.

Section 210. Rule of construction

Section 210 provides that the bill shall not be construed so as to limit the scope or applicability of the Commodity Exchange Act.

SUBTITLE B—BANK INVESTMENT COMPANY ACTIVITIES

Section 211. Custody of investment company assets by affiliated banks

Section 211(a) reorganizes Section 17(f) of the Investment Company Act of 1940 and adds a new paragraph 17(f)(6). New paragraph 17(f)(6) authorizes the Commission to adopt rules prescribing the conditions under which a bank or an affiliate of a bank, when either of them is affiliated with an investment company, may serve as custodian of that investment company.

Section 211(b) similarly amends Section 26 of the Investment Company Act to add a new subsection 26(b). New subsection 26(b) authorizes the Commission to adopt rules prescribing the conditions under which a bank or an affiliate of a bank, when either of them is affiliated with a unit investment trust, may serve as custodian of that unit investment trust.

Section 211(c) amends Section 36(a) of the Investment Company Act to add a new paragraph 36(a)(3). Section 36(a) currently authorizes the Commission to bring actions for breach of fiduciary duty against the officers, directors, investment advisers, and principal underwriters of an investment company. New paragraph 36(a)(3) provides the Commission with the authority to bring an action for breach of fiduciary duty against a custodian of an investment company as well.

Section 212. Lending to an affiliated investment company

Section 212 amends Section 17(a) of the Investment Company Act to add a new paragraph 17(a)(4). Section 17(a) currently makes it unlawful for any affiliated person, promoter, or principal underwriter of an investment company to sell any security or other property to the investment company (subject to certain exceptions), to purchase any security or other property from the investment company (except securities of the investment company), or to borrow money or other property from the investment company (except as permitted by Section 21(b)). New paragraph 17(a)(4) makes it unlawful for any affiliated person, promoter, or principal underwriter of an investment company to lend money or other property to the investment company in contravention of such rules as the Commission may promulgate.

Section 213. Independent directors

Section 213(a) amends Section 2(a)(19)(A) of the Investment Company Act. Section 2(a)(19)(A)(v) defines an "interested person" of an investment company to include any broker or dealer registered under the Securities Exchange Act and any affiliated person of such a broker or dealer. Section 213(a) replaces Section 2(a)(19)(A)(v) with new Section 2(a)(19)(A)(v) and (vi). New Section 2(a)(19)(A)(v) defines an "interested person" of an investment company as any person or affiliate of a person who during the preceding six-month period has executed any portfolio transactions for the investment company or any related investment company. New Section 2(a)(19)(A)(vi) defines an "interested person" of an investment company as any person or affiliate of a person who during the preceding six-month period has loaned money or other property to the investment company or any related investment company. Section 213(b) makes a conforming change to Section 2(a)(19)(B) of the Investment Company Act, which defines an "interested person" of an investment adviser or principal underwriter of an investment company.

Section 213(c) amends Section 10(c) of the Investment Company Act. Section 10(c) generally provides that no investment company may have a majority of its board of directors consisting of officers, directors, or employees of any one bank. Section 213(c) extends this prohibition to the officers, directors, or employees of any one bank or bank holding company, together with the bank or bank holding company's affiliates and subsidiaries.

Section 213(d) provides that the amendments made by Section 213 shall take effect one year after the date of enactment.

Section 214. Additional SEC disclosure authority

Section 214 amends Section 35(a) of the Investment Company Act. Section 35(a) currently makes it unlawful for any person issuing or selling any security of an investment company to represent or imply in any manner that such security or company is guaranteed, sponsored, recommended, or approved by the United States or any agency, instrumentality or officer thereof. New Section 35(a) further makes it unlawful for any person issuing or selling any security of an investment company to represent or imply in any manner that such security or company is insured by the FDIC or is guaranteed by or is an obligation of any bank.

New Section 35(a) further requires any person issuing or selling the securities of an investment company that is advised by, or sold through, a bank to disclose prominently that an investment in the company is not insured by the FDIC or any other government agency. The Commission is given authority to issue rules prescribing the manner in which this disclosure will be provided.

Section 215. Definition of broker under the Investment Company Act of 1940

Section 215 amends Section 2(a)(6) of the Investment Company Act. Section 2(a)(6) defines "broker" for purposes of the Investment Company Act and currently contains an exemption for banks. New Section 2(a)(6) defines "broker" as having the same meaning as in the Securities Exchange Act, except that for purposes of the Investment Company Act it does not include any person solely by reason of the fact that such person is an underwriter for one or more investment companies. The exemption for banks is deleted.

Section 216. Definition of dealer under the Investment Company Act of 1940

Section 216 amends Section 2(a)(11) of the Investment Company Act. Section 2(a)(11) defines "dealer" for purposes of the Investment Company Act and currently contains an exemption for banks. New Section 2(a)(11) defines "dealer" as having the same meaning as in the Securities Exchange Act, except that for purposes of the Investment Company Act it does not include any insurance company or investment company. The exemption for banks is deleted.

Section 217. Removal of the exclusion from the definition of investment adviser for banks that advise investment companies

Section 217(a) amends Section 202(a)(11) of the Investment Advisers Act of 1940. Section 202(a)(11) defines "investment adviser" and currently exempts any bank or bank holding company that is not an investment company. New Section 202(a)(11) removes this exemption for any bank or bank holding company to the extent it serves or acts as an investment adviser to an investment company. If such services or actions performed through a separately identifiable department or division of a bank, the department or division and not the bank itself shall be deemed to be the investment adviser.

Section 217(b) adds a new Section 202(a)(26) to the Investment Advisers Act. New Section 202(a)(26) defines "separately identifiable department or division" of a bank as a unit under the direct supervision of an officer or officers designated by the bank's directors as responsible for the day-to-day conduct of the bank's investment adviser activities for one or more investment companies, including the supervision of all bank employees engaged in the performance of such activities. All records relating to investment adviser activities must be separately maintained in or extractable from the unit's own facilities or the facilities of the bank so as to permit examination and enforcement by the Commission.

Section 218. Definition of broker under the Investment Advisers Act of 1940

Section 218 amends Section 202(a)(3) of the Investment Advisers Act. Section 202(a)(3) defines "broker" for purposes of the Investment Advisers Act and currently contains a blanket exemption for banks. New Section 202(a)(3) defines "broker" as having the same meaning as in the Securities Exchange Act. The blanket exemption for banks is deleted.

Section 219. Definition of dealer under the Investment Advisers Act of 1940

Section 219 amends Section 202(a)(7) of the Investment Advisers Act. Section 202(a)(7) defines "dealer" for purposes of the Investment Advisers Act and currently contains a blanket exemption for banks. New Section 202(a)(7) defines "dealer" as having the same meaning as in the Securities Exchange Act, except that for purposes of the Investment Advisers Act it does not include any insurance company or investment company. The blanket exemption for banks is deleted.

Section 220. Interagency consultation

Section 220 amends the Investment Advisers Act to add a new Section 210A. New Section 210A authorizes the Commission to receive from a Federal banking agency the results of any examination, reports, records, or other information to which such agency may have access regarding the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of a bank, that is registered as an investment adviser or that has a subsidiary or separately identifiable department or division registered as an investment adviser. New Section 210A similarly authorizes the Federal banking agencies to receive from the Commission the results of any examination, reports, records, or other information regarding the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of a bank, that is registered as an investment adviser. Section 210A does not limit the authority of any Federal banking agency with respect to such bank holding company, bank, or separately identifiable department or division under any provision of law.

Section 221. Treatment of bank common trust funds

Section 221(a) amends Section 3(a)(2) of the Securities Act of 1933. Section 3(a)(2) currently exempts from the application of the Securities Act any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed by the bank in its capacity as trustee, executor, administrator, or guardian. As amended, Section 3(a)(2) exempts any interest or participation in any common trust fund or similar fund that is excluded from the definition of "investment company" under new Section 3(c)(3) of the Investment Company Act.

Section 221(b) similarly amends Section 3(a)(12)(A)(iii) of the Securities Exchange Act of 1934. Section 3(a)(12)(A)(iii) currently exempts from the application of the Securities Exchange Act any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed by the bank in its capacity as trustee, executor, administrator, or guardian. As amended, Section 3(a)(12)(A)(iii) exempts any interest or participation in any common trust fund or similar fund that is excluded from the definition of "investment company" under new Section 3(c)(3) of the Investment Company Act.

Section 221(c) amends Section 3(c)(3) of the Investment Company Act. Section 3(c)(3) currently exempts from the definition of "investment company" any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed by the bank in its capacity as trustee, executor, administrator, or guardian. As amended, Section 3(c)(3) exempts such a bank common trust fund only if (i) the fund is employed by the bank solely as an aid to the administration of trusts, estates, or other fiduciary accounts; (ii) interests in the fund are not advertised or offered for sale to the general public, except in connection with the ordinary advertising of the bank's fiduciary services; and (iii) fees and expenses charged by the fund are in keeping with fiduciary principles established under applicable Federal or State law.

Section 222. Investment advisers prohibited from having controlling interest in registered investment company

Section 222 amends Section 15 of the Investment Company Act to add a new subsection 15(g). Section 15 regulates advisory contracts between investment companies and their investment advisers. New subsection 15(g) requires that if an investment adviser, or an affiliated person of that adviser, holds a controlling interest in an investment company in a trustee or fiduciary capacity, he or she must transfer the power to vote the shares of the investment company. If the adviser or an affiliate holds the shares in a trustee or fiduciary capacity under an employee benefit plan subject to the Employee Retirement Income Security Act of 1974, he or she must transfer the power to vote the shares of the investment company to another plan fiduciary who is not affiliated with the adviser or an affiliate. If the adviser or an affiliate holds the shares in a trustee or fiduciary capacity under any other circumstance, he or she must either (i) transfer the power to vote the shares of the investment company to the beneficial owners, to another fiduciary who is not affiliated with the adviser or an affiliate, or to any person authorized to receive statements and information with respect to the trust who is not affiliated with the adviser or an affiliate; (ii) vote the shares of the investment company in the same proportion as shares held by all other shareholders of the investment company; or (iii) vote the shares of the investment company as otherwise permitted by such rules as the Commission may prescribe. Acting in accordance with these provisions is deemed not to breach a fiduciary duty under State or Federal law. These provisions do not apply if the investment company consists solely of assets held in a trustee or fiduciary capacity.

Section 223. Conforming change in definition

Section 223 amends Section 2(a)(5) of the Investment Company Act. Section 2(a)(5) defines "bank" for purposes of the Investment Company Act to include any banking institution organized under the laws of the United States. As amended, Section 2(a)(5) defines "bank" to include any depository institution as defined in Section 3 of the Federal Deposit Insurance Act and any branch or agency of a foreign bank as defined in Section 1(b) of the International Banking Act of 1978.

Section 224. Conforming amendment

Section 224 amends Section 202 of the Investment Advisers Act to add a new subsection 202(c). New subsection 202(c) requires the Commission, whenever it is engaged in rulemaking or is required to consider or determine whether an action is necessary or appropriate in the public interest, under the Investment Advisers Act, to consider the promotion of efficiency, competition, and capital formation as well as the protection of investors. Similar changes were made to the Securities Act, the Securities Exchange Act, and the Investment Company Act by the National Securities Markets Improvement Act of 1996.

Section 225. Effective date

Section 225 provides that this subtitle shall take effect 90 days after the date of enactment.

SUBTITLE C—SECURITIES AND EXCHANGE COMMISSION SUPERVISION OF INVESTMENT BANK HOLDING COMPANIES

Section 231. Supervision of investment bank holding companies by the Securities and Exchange Commission

Section 231 establishes a supervised investment bank holding company ("IBHC'), as an alternative to a financial holding company. An IBHC must register with, and is supervised by, the Commission. This alternative is made available to any company that controls two or more broker-dealers and is not affiliated with a WFI, an insured bank or savings association, or certain foreign banks and companies. An IBHC may affiliate with uninsured trust companies, credit card banks, Edge Act companies, CEBA institutions, and foreign branches of National banks. This section outlines registration, discontinuation, and record keeping requirements for

IBHCs. This section provides the Commission with examination authority and the power to regulate the IBHC's capital if deemed necessary. The Commission is required to defer to the appropriate regulator regarding the interpretation of banking or insurance law with respect to the banking and insurance activities of the IBHC. Finally, the Commission is granted "backup" supervisory authority over certain WFHCs to ensure that the WFHC and its affiliates comply with Federal securities law.

SUBTITLE D—STUDY

Section 241. Study of methods to inform investors and consumers of uninsured products

Section 241 mandates a GAO study of the efficacy, costs, and benefits of requiring insured depository institutions to inform consumers through the use of a logo or seal that a securities or insurance product is not FDIC-insured.

Section 242. Study of limitation on fees associated with acquiring financial products

Section 242 requires the GAO to undertake a study of the efficacy and benefits of uniformly limiting costs associated with the purchase of a financial product.

Title III—Insurance

SUBTITLE A—STATE REGULATION OF INSURANCE

Section 301. State regulation of the business of insurance

Section 301 states that the McCarran-Ferguson Act (15 U.S.C. Sec. 1011 et seq.) remains the law of the United States.

Section 302. Mandatory insurance licensing requirements

Section 302 provides that, subject to Section 104, any person providing insurance in a State as principal or agent must be licensed as required by the appropriate insurance regulator of such State.

Section 303. Functional regulation of insurance

Section 303 provides that, subject to Section 104, the insurance sales activities of any person or entity shall be functionally regulated by the States. Section 104 establishes a safe harbor for State regulation of insurance sales, as well as a method for determining whether State regulation falling outside the safe harbor would be pre-empted.

Section 304. Insurance underwriting in National banks

Section 304(a) prohibits National banks and their subsidiaries from providing insurance in a State as principal. This prohibition does not apply to "authorized products." Under Section 304(b), a product is "authorized" if, as of January 1, 1997, National banks were lawfully providing it as principal or the Comptroller of the Currency had determined in writing that National banks may provide it as principal; no court of relevant jurisdiction had, by final judgment, overturned a determination by the Comptroller that National banks may provide it as principal; and the product is not title insurance or an annuity contract subject to tax treatment under Section 72 of the Internal Revenue Code.

Section 304(c) defines "insurance" for purposes of Section 304. Under Section 304(c)(1), "insurance" means any product regulated as insurance as of January 1, 1997 in the State in which the product is provided. Under Section 304(c)(2), insurance means any product first offered after January 1, 1997 which a State insurance regulator determines shall be regulated as insurance in the State in which the product is provided because the product insures, guarantees, or indemnifies against loss of life, loss of health, or loss through damage to or destruction of property. Products which may not be a product or service of a bank that is a deposit product are (i) a loan, discount, letter of credit, or other extension of credit; (ii) a trust or other fiduciary service; (iii) a qualified financial contract as defined in Section 11(e)(8)(D)(I) of the Federal Deposit Insurance Act; or (iv) a financial guaranty; except a bank product does not include a product that has an insurance component such that if offered by a bank as principal the product would be treated as a life insurance contract under Section 7702 of the Internal Revenue Code or losses incurred with respect to the product would qualify for treatment under Section 832(b)(5) of the Internal Revenue Code if the bank were subject to tax as an insurance company under Section 832 of the Internal Revenue Code. The term "financial guaranty" in Section 304(c)(2)(B)(v) is not intended to exclude surety bonds from the definition of insurance. Under Section 304(c)(3), insurance means any annuity contract on which the income is subject to tax under Section 72 of the Internal Revenue Code.

Section 305. Title insurance activities of National banks and their affiliates

Section 305(a) prohibits National banks and their subsidiaries from engaging in any activity involving the underwriting of title insurance, other than title insurance underwriting activities in which they were lawfully engaged before the date of enactment. Section 305(b) provides that, in the case of a National bank that has an affiliate which provides insurance as principal, neither the bank nor a subsidiary of the bank may engage in any activity involving the underwriting of title insurance. Section 305(c) provides that, in the case of a National bank that has a subsidiary that provides insurance as principal and no affiliate that provides insurance as principal, the bank may not engage in any activity involving the underwriting of title insurance.

Section 306. Expedited and equalized dispute resolution for financial regulators

Section 306(a) provides that in the event of a regulatory conflict between a State insurance regulator and a Federal regulator as to whether a product is insurance as defined in Section 304(c), or as to whether a State statute, regulation, order, or interpretation regarding insurance sales or solicitation activity is preempted under Federal law, either regulator may seek expedited judicial review. Either regulator may file a petition for review in the U.S. Court of Appeals for the District of Columbia Circuit or in the U.S. Court of Appeals for the circuit in which the State is located.

Under Section 306(b), the relevant U.S. Court of Appeals must complete all action on the petition, including rendering a judgment, within 60 days from the filing of the petition unless all parties agree to an extension. Under Section 306(c), any request for certiorari to the U.S. Supreme Court must be filed as soon as practicable after the judgment of the U.S. Court of Appeals is issued. Section 306(d) provides that no action challenging an order, ruling, determination, or other action of a Federal or State regulator may be brought under these procedures after the later of (i) 12-months after the first public notice of the order, ruling, or determination in its final form, or (ii) 6-months period after the order, ruling, or determination takes effect.

Section 306(e) requires the court to base its decision on an action filed under this section upon its review on the merits of all questions presented under Federal and State law. The court must review the nature of the product or activity and the history and purpose of its regulation under Federal and State law. The court may not accord unequal deference to either regulator.

Section 307. Consumer protection regulations

Section 307 adds a new Section 45 to the Federal Deposit Insurance Act. New Section 45(a) directs the Federal banking regulators, within one year of the date of enactment of this Act, to prescribe consumer protection regulations that the regulators jointly determine to be appropriate. The regulations will apply to retail sales practices, solicitations, advertising, or offers of any insurance product by any insured depository institution or wholesale financial institution or any person engaged in such activities at an office of, or on behalf of, such an institution. The regulations must be consistent with the requirements of this Act and provide such additional consumer protections as the regulators determine to be appropriate. The regulations must apply to subsidiaries of insured depository institutions as deemed appropriate by the regulators to protect consumers. In prescribing the regulations, the Federal banking regulators must consult with the State insurance regulators, as appropriate.

New Section 45(b) requires the regulations prescribed pursuant to new Section 45(a) to include anti-coercion rules applicable to the sale of insurance products. The anti-coercion rules must prohibit an insured depository institution from engaging in any practice that would lead a consumer to believe that an extension of credit, in violation of Section 106(b) of the Bank Holding Company Act Amendments of 1970, is conditional upon (i) the purchase of an insurance product from the institution, its affiliates or subsidiaries; or (ii) an agreement by the consumer not to obtain, or a prohibition on the consumer from obtaining, an insurance product from an unaffiliated entity.

New Section 45(c) requires the regulations to include certain provisions relating to disclosures and advertising in connection with the initial purchase of an insurance product. The regulations must require oral and written disclosure, before completion of the initial sale, that the product is not insured by the FDIC, the U.S. government, nor the insured depository institution; and in the case of an insurance product such as a variable annuity that involves an investment risk, that there is an investment risk associated with the product, including possible loss of value. Oral and written disclosure must be made before completion of the initial sale and at the time of application for an extension of credit that approval of an extension of credit may not be conditioned on the purchase of an insurance product from the lending institution or its affiliates or subsidiaries; nor on an agreement by the consumer not to obtain, or a prohibition on the consumer from obtaining, an insurance product from an unaffiliated entity.

The regulations must encourage the use of conspicuous, simple, direct, and readily understandable disclosure. Examples of such disclosure include: NOT FDIC-INSURED; NOT GUARANTEED BY THE BANK; MAY GO DOWN IN VALUE. The regulations must require an insured depository institution to obtain an acknowledgment by the consumer of the receipt of the required disclosure at the time the consumer receives the disclosure or at the time of the consumer's initial purchase of the product. The regulations shall make necessary adjustments for purchases in person, by telephone, or by electronic media to provide for appropriate and complete disclosure and acknowledgment.

The regulations must prohibit any practice or advertising at any office of, or on behalf of, an insured depository institution or its subsidiary which could mislead any person or otherwise cause a reasonable person to reach an erroneous belief with respect to the uninsured nature of any insurance product sold or offered for sale, or, in the case of an insurance product such as a variable annuity which involves an investment risk, the investment risk associated with such product.

New Section 45(d) provides that the regulations must include such provisions as the Federal banking regulators deem appropriate to ensure that the routine acceptance of deposits is, to the extent practicable, kept physically segregated from insurance product activity. The regulations must clearly delineate the setting in which, and the circumstances under which, transactions involving insurance products should be conducted in a location physically segregated from an area where retail deposits are routinely accepted. The regulations must include standards that permit a person accepting deposits from the public in an area where such transactions are routinely conducted to receive a one-time nominal fee of a fixed dollar amount for each referral of a customer seeking to purchase an insurance product to a qualified person who sells such product. The fee may not depend on whether the referral results in a transaction. The regulations also must prohibit any person from selling or offering for sale an insurance product in any part of any office of an insured depository institution, or on the institution's behalf, unless the person is appropriately qualified and licensed.

New Section 45(e) prohibits discrimination against victims of domestic violence and providers of services to victims of domestic violence as applicants for, or as insureds under, any insurance product sold or offered for sale, as principal, agent, or broker, by, at, or on behalf of, an insured depository institution. "Domestic violence" is defined as certain actions by a current or former family member, household member, intimate partner, or caretaker. The actions are:

(i) attempting to cause, causing or threatening physical harm, severe emotional distress, psychological trauma, rape or sexual assault; (ii) engaging in a course of conduct or repeatedly committing acts, including following a person without proper authority, under circumstances that place the person in reasonable fear of bodily injury or physical harm; (iii) subjecting a person to false imprisonment; and (iv) attempting to cause, or causing damage to, property so as to intimidate or attempt to control the behavior of another person. New Section 45(e) expresses the sense of the Congress that, within 30 months after the date of enactment, States should enact prohibitions against discrimination against victims of domestic violence and providers of services to victims of domestic violence as applicants for, or as insureds under, any insurance product.

New Section 45(f) requires the Federal banking agencies to jointly establish a consumer complaint mechanism for receiving and expeditiously addressing consumer complaints alleging violations of the regulations issued under this section. The Federal banking agencies must establish a group within each agency to receive such complaints; develop investigative procedures; develop procedures for informing consumers of their rights; and develop procedures for addressing complaints and recovering losses.

New Section 45(g) provides that no provision of new Section 45 shall be construed as affecting (i) any authority of the Commission, any self-regulatory organization, the Municipal Securities Rulemaking Board, or the Secretary of the Treasury under any Federal securities law; or (ii) any authority of any State insurance commissioner or other State authority under any State law. New Section 45(g) further provides that regulations promulgated under this section will not apply in a State which has in effect statutes, regulations, orders, or interpretations that are inconsistent with or contrary to the regulations. However, a provision of the regulations prescribed under this section shall supersede the comparable provision of State law if the Federal banking agencies jointly determine that the protection afforded to consumers by such provision is greater than that provided by the State law.

New Section 45(h) provides that, for purposes of this section, the term "insurance product" includes an annuity contract subject to tax treatment under Section 72 of the Internal Revenue Code.

Section 308. Certain State affiliation laws preempted for insurance companies and affiliates

Section 308 provides that, except as provided in Section 104(a)(2), no State may prevent or significantly interfere with the ability of an insurer, or any affiliate of an insurer, to become a financial holding company or to acquire control of an insured depository institution. Section 308 further provides that no State may limit the amount of an insurer's assets that may be invested in the voting securities of insured depository institution or a company that controls such an institution, except the State of the insurer's domicile may limit the investment to 5 percent of the insurers assets. Section 308 further provides that no State other than the State of the insurer's domicile may prevent, significantly interfere with, review, approve, or disapprove of an insurer's plan of reorganization from mutual form to stock form.

SUBTITLE B—NATIONAL ASSOCIATION OF REGISTERED AGENTS AND BROKERS

Section 321. State flexibility in multistate licensing reforms

Section 321 provides that Subtitle B will take effect unless three years after the date of enactment of the Act a majority of the States have enacted uniform laws and regulations governing licensing insurance agent and agencies, or have enacted reciprocity laws and regulations governing the licensing of nonresident agents and agencies.

Section 322. National Association of Registered Agents and Brokers

Section 322 establishes the National Association of Registered Agents and Brokers (NARAB), a nonprofit corporation that is not an agency of the United States.

Section 323. Purpose

Section 323 states that NARAB's purpose is to provide a mechanism through which uniform licensing, appointment, continuing education, and other qualifications and conditions can be adopted and applied on a multistate basis. NARAB must preserve the rights of States to license, supervise, and discipline insurance producers and to prescribe and enforce laws and regulations relating to insurance-related consumer protection and unfair trade practices.

Section 324. Relationship to the Federal Government

Section 324 states that NARAB will be subject to the supervision and oversight of the National Association of Insurance Commissioners and is not an agency or instrumentality of the United States Government.

Section 325. Membership

Section 325 provides that any State-licensed insurance producer is eligible to be a member of NARAB.

Section 326. Board of directors

Section 326 states that NARAB will have a board of directors composed of 7 members serving three-year terms appointed by the National Association of Insurance Commissioners. At least four of the board members must have significant experience with the regulation of commercial lines of insurance in at least one of the 20 States with the greatest total dollar amount of commercial-lines insurance in the United States.

Section 327. Officers

Section 327 establishes the officers of NARAB: Board Chairperson (who must be a member of the National Association of Insurance Commissioners), Board Vice Chairperson, President, Secretary, and Treasurer. It requires each officer of the Board and NARAB to be elected for a three-year term.

Section 328. Bylaws, rules and disciplinary actions

Section 328 describes the procedure for adoption and amendment of the bylaws and rules and details determinations as to whether any membership should be denied, suspended, revoked, or not renewed.

Section 329. Assessments

Section 329 authorizes NARAB to assess application and membership fees necessary to cover the costs of its operations provided that it does not discriminate against smaller insurance producers. Section 329 also authorizes the National Association of Insurance Commissioners (NAIC) to assess the NARAB for any costs it incurs under Subtitle B.

Section 330. Functions of the NAIC

Section 330 authorizes the National Association of Insurance Commissioners to examine and inspect NARAB and require NARAB to file reports appropriate to the public interest. It requires NARAB to annually report to the NAIC about its business, financial condition, and related matters. NAIC will transmit the report to Congress and the President. It further provides that rulemaking determinations made by NAIC pursuant to Section 328 must be made after offering a notice and comment period and an opportunity for a hearing.

Section 331. Liability of the association and the directors, officers, and employees of the association

Section 331 states that NARAB is not to be deemed an insurer or insurance producer under State law. It provides that NARAB and its officers, directors, and employees are immune from liability for any action taken or omitted in good faith under or in connection with any matter in Subtitle B.

Section 332. Elimination of NAIC oversight

Section 332 contains provisions for establishing NARAB without National Association of Insurance Commissioners oversight under certain circumstances.

Section 333. Relationship to State law

Section 333 describes circumstances under which State laws and actions purporting to regulate insurance producers will be preempted.

Section 334. Coordination with other regulators

Section 334 authorizes NARAB to issue uniform insurance producer applications and renewal applications; establish a central clearinghouse through which NARAB members may apply for new or renewal of licenses; and establish a national database of regulatory information on insurance producers.

Section 335. Judicial review

Section 335 sets standards of review, requires an aggrieved individual to exhaust all available administrative remedies before NARAB and the NAIC before seeking judicial review of a NARAB decision, and identifies the courts with appropriate jurisdiction over litigation involving NARAB.

Section 336. Definitions

Section 336 defines “insurance,” “insurance producer,” “State law,” “State” and “home state.”

Title IV—Unitary Savings and Loan Holding Companies

Section 401. Prevention of creation of new S&L holding companies with commercial affiliates

Section 401 prohibits any company that engages, directly or through a subsidiary, in commercial activities from directly, or indirectly, acquiring control of a savings association after September 3, 1998. Section 401 also prohibits any savings and loan holding company from engaging directly, or through a subsidiary, in commercial activities. Certain existing unitary savings and loan holding companies are exempted from these restrictions. In particular, these prohibitions do not apply to a unitary savings and loan holding company in existence on September 3, 1998, or that was formed pursuant to applications pending before the OTS on or before that date, provided that the company continues to meet the requirements to be a unitary savings and loan holding company under 12 U.S.C. 1467a(c)(3) and controls at least one of the savings associations that the company controlled (or had applied to control) as of September 3, 1998, or the successor to such a savings association (a “grandfathered unitary savings and loan holding company”).

The purpose of Section 401 is to prohibit any company directly or indirectly engaged in commercial activities (other than a grandfathered unitary savings and loan holding company) from acquiring control of a savings association after September 3, 1998, by or through any means including through any forward or reverse merger, consolidation, or other type of business combination. Section 401 authorizes the OTS to issue such regulations, interpretations, and orders as may be necessary to prevent evasions of this prohibition, and the Committee expects the OTS to take all actions necessary to carry out the purpose of this section, which is to prohibit firms engaged in commercial activities from acquiring control of any savings associations.

In making such determinations or taking other actions under Section 401, the OTS should use the definition of “control” set forth in Section 10 of the Home Owners’ Loan Act.

Section 402. Optional conversion of Federal savings associations to National banks

Section 402 permits Federal savings associations, or branches thereof in any State, to convert to National banks with the approval of the Comptroller of the Currency provided that they meet all of the requirements for a National bank. The new banks would have to apply to the FDIC for deposit insurance. Statutory requirements for any payment of exit fees by any insured depository institution leaving a deposit insurance fund would not be affected by this section.

Section 403. Retention of "Federal" in name of converted Federal savings association

Section 403 would permit Federal savings associations that convert to National or State bank charters to keep the word "Federal" in their names. For example, if First Federal Savings Bank converts from a Federal savings association to a State bank charter, it may retain its former name.

Title V—Financial Information Privacy

Section 501. Financial information privacy

Section 501 makes it unlawful to obtain or attempt to obtain, or cause to be disclosed, or attempt to cause to be disclosed, customer information of a financial institution through fraudulent or deceptive means; such as by misrepresenting the identity of the person requesting the information or otherwise tricking an institution or customer into making unwitting disclosures of such information. This section also makes it unlawful to request that customer financial information be obtained knowing, or consciously avoiding knowing, that the information will be collected in a fraudulent or deceptive manner. This section exempts from coverage law enforcement agencies that acquire customer information from a financial institution in carrying out their official duties and financial institutions engaged in efforts to combat fraud such as tests of security systems for maintaining the confidentiality of customer information and investigations of allegations of employee misconduct.

Section 502. Report to Congress on financial privacy

Section 502 requires the GAO to report to Congress within eighteen months of enactment on the efficacy and adequacy of this provision and recommend whether additional legislation or regulations are needed.

Title VI—Miscellaneous

Section 601. Grand jury proceedings

Section 601 permits U.S. Attorneys offices to seek a court order to provide financial institution regulatory agencies with access to grand jury material giving State regulatory agencies parity with Federal regulatory agencies.

Section 602. Sense of the Committee on Banking, Housing, and Urban Affairs of the Senate

Section 602 expresses the Sense of the Committee that legislation should be enacted to reduce the tax burden on community banks by expanding the availability of the Subchapter S tax election.

Section 603. Investments in government sponsored enterprises

Section 603 amends the Federal Deposit Insurance Act to allow a holding corporation (formerly a government sponsored enterprise, "GSE") that was privatized by Federal legislation to enter into an affiliation arrangement with an insured depository institution provided that the Secretary of the Treasury approves the affiliation and determines that the successful wind-down of the GSE will not be affected and that the GSE will otherwise be separate from the arrangement. The Secretary of the Treasury is authorized to impose any conditions on the affiliation that the Secretary deems appropriate.

Section 604. Repeal of savings bank provisions in the Bank Holding Company Act of 1956

Section 604 repeals section 3(f) of the Bank Holding Company Act to conform the regulation of savings bank life insurance with the regulations governing all other financial institutions in a bank holding company structure.

REGULATORY IMPACT STATEMENT

In accordance with paragraph 11(g), rule XXVI of the Standing Rules of the Senate, the Committee makes the following statement regarding the regulatory impact of the bill.

The bill establishes a comprehensive framework to permit affiliations between banks, securities firms and insurance companies. It would modernize and reform outdated laws governing the financial system. The new framework promotes competition, enhances consumer choice, safeguards the Federal deposit insurance system, and protects the safety and soundness of insured depository institutions and the stability of the payment system.

The bill reduces substantially the current regulatory burdens placed on financial intermediaries—banks, broker-dealers, insurance and securities firms—in several ways. First, the bill incorporates the principle of functional regulation. By clearly allocating regulatory responsibility to Federal and State financial regulators, the proposed system of functional regulation promotes efficiency, eliminates regulatory overlap and duplication, and promotes increased investor, depositor and taxpayer protections.

Second, the bill streamlines the regulatory process by requiring coordination and information-sharing between the various Federal and State regulators. The bill seeks to provide regulation of financial holding companies that is sufficient to protect the safety and soundness of the financial system and the integrity of the Federal Deposit insurance funds without imposing unnecessary regulatory burdens.

Third, the bill eliminates many notification and approval procedures mandated under current law. Because the bill seeks to streamline and update the financial regulatory framework, the Committee believes that this legislation will have a favorable regulatory impact.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

Senate rule XXVI, section 11(b) of the Standing Rules of the Senate, and Section 403 of the Congressional Budget Impoundment and Control Act, require that each committee report on a bill containing a statement estimating the cost of the proposed legislation, which was prepared by the Congressional Budget Office. This statement has been requested from the Congressional Budget Office, but it was not available at the date of filing this report. When the information is made available to the Committee, it will be placed in the Congressional Record.

CHANGES IN EXISTING LAW

In the opinion of the Committee, it is necessary to dispense with the requirement of section 12 of rule XXVI of the Standing Rules of the Senate in order to expedite the business of the Senate.

ADDITIONAL VIEWS OF SENATOR CONNIE MACK

I am committed to moving this bill forward, however, I still have concerns about the language which was included in the managers' amendment regarding the application of the Community Reinvestment Act (CRA) to Wholesale Financial Institutions (referred to as "woofies") and the ability of the Federal Reserve to impose limitations on new activities of financial services holding companies. I view these provisions as expanding CRA.

I do not support the Community Reinvestment Act as it has evolved, and I oppose subjecting any industry to these requirements. In fact, I would prefer to see the entire Community Reinvestment Act repealed. Because of CRA, banks are now often forced to make unsound and risky loans in economically disadvantaged areas. If they do not make these high risk investments, they are accused of discrimination. I strongly believe that most of these allegations are false.

In contrast to banks, WFIs will not be permitted to accept retail deposits under $100,000, and will not have federal deposit insurance. When the Community Reinvestment Act was enacted, CRA was the price banks were to pay for federal deposit insurance. Why should this price be imposed on an entity which can not qualify for deposit insurance?

In this legislation, the CRA provision is one of the most difficult things to accept. I was once in the banking business, and had to deal with the burdens of CRA. Philosophically, I agree with Senators Gramm and Shelby that this bill's expansion of CRA, regardless of how harmless it may appear, is wrong. Senator Gramm proposed two amendments that I would have liked to support, but I know if his amendments were incorporated into the bill, the likelihood of this becoming law would be greatly diminished. For that reason, and because of the efforts that have been made to find compromise, I found myself in a position that, frankly, I didn't like. I believe, for the sake of compromise, and the need to have this bill go forward, I would have had to vote against Senator Gramm's amendments which would have lessened the burdens of CRA.

H.R. 10, as it came over from the House, contained six provisions referring to or expanding the Community Reinvestment Act. At this time, in the name of compromise, I am willing to withhold my objections to the CRA provisions in the bill. I am pleased that the CRA compromise in the managers' amendment deletes many of the provisions which I found offensive. These provisions required divestiture due to unsatisfactory CRA ratings, applied CRA to foreign banks, and directed the Treasury to conduct a study on CRA. I believe the included compromise on CRA has moved in the right direction, but we still have some work to ensure that H.R. 10 is "CRA-neutral."

As this bill moves through the legislative process, I will continue to work with my colleagues on additional compromises to move this bill towards CRA neutrality. My support of this bill is due to the compromises incorporated in the manager's amendment. I would like to thank my colleagues for their willingness to work out a compromise on so many complicated issues. I hope we will be able to continue discussing the CRA issue prior to floor consideration.

CONNIE MACK.

ADDITIONAL VIEWS OF WAYNE ALLARD

I support this financial modernization legislation. The legislation is not perfect, but the Committee has worked hard to reach a consensus on important issues. Financial modernization will increase competition and benefit the economy.

I am always concerned with the impact of banking legislation on community bankers. Financial modernization should benefit small financial institutions as well as large financial institutions. I am therefore pleased that the Committee has included language supporting the small bank tax relief legislation that I have proposed. This legislation would expand the Subchapter S tax election available to financial institutions.

Subchapter S of the Internal Revenue Code was first enacted in 1958 to reduce the tax burden on small business corporations. The Subchapter S provisions have been liberalized a number of times over the last two decades, most significantly in 1982, and again in 1996. This liberalization reflects a desire on the part of Congress to relieve the tax burden on small business. S corporations do not pay corporate level income taxes, earnings are passed through to the shareholder level where income taxes are paid, thus eliminating the double taxation of corporations. By contrast, Subchapter C corporations pay corporate level income taxes on earnings, and shareholders pay income taxes again on those same earnings when they are passed through as dividends.

Congress made the S corporation option available to small banks for the first time in the 1996 "Small Business Job Protection Act." Since then, ten percent of FDIC insured financial institutions have converted to Subchapter S corporations, and eighty percent of these have assets under $100 million. Unfortunately, many small banks which would like to convert to Subchapter S are having trouble qualifying under the current rules. The Sense of the Committee language therefore recommends enactment of legislation to increase the allowed number of S corporation shareholders; permit S corporation stock to be held in individual retirement accounts; clarify that interest on investments held by banks for safety, soundness, and liquidity purposes should not be considered to be passive income; provide that bank director stock is not treated as a disqualifying second class of stock; and improve the tax treatment of bad debt and interest deductions for financial institutions.

WAYNE ALLARD.

ADDITIONAL VIEWS OF SENATOR ROD GRAMS

Notwithstanding my opposition to certain provisions in H.R. 10, I want to reiterate my enthusiastic support for financial modernization. As one of the Senate's strongest and most consistent supporters of financial modernization, I believe that Congress, not the regulators, should lead in modernizing the nation's financial laws because modernization via regulatory fiat results in convoluted rules which are open to perpetual interpretation and continual litigation. However, as has been the case on so many instances, Congress is showing up to the dance after the music has ended.

I am pleased that H.R. 10 provides core financial modernization provisions—such as repealing the Glass-Steagall Act and allowing banks and insurance companies to affiliate. By repealing the Glass-Steagall Act, Congress deletes an obsolete statute which was arguably misguided when it was originally enacted. Also, by removing the Bank Holding Company Act prohibition on common ownership of banks and insurance companies, the bill allows true one-stop shopping for individuals financial needs. Also, although not perfect, the bill includes a good insurance regulation framework from which to work.

However, there are a number of flaws in H.R. 10 which may well result in its demise. The first fatal flaw in this legislation is the broad expansion of the Community Reinvestment Act (CRA). A statement in the Congressional Record by the bill's author, Senator William Proxmire, when he introduced the CRA argued that one of the assumptions—or justifications—for the CRA is that a bank or thrift charter conveys "economic benefit." Of those listed in the Senator's statement, one of the only remaining economic benefits is government provided deposit insurance. Although the reach of the CRA has always been limited to insured depository institutions, H.R. 10, for the first time, extends the CRA to uninsured wholesale financial institutions (WFI).

Another flaw of H.R. 10 is the treatment of the unitary thrift holding company. There is a broad disagreement over how and if the affiliation right of unitary thrift holding companies should be limited. Under current law, unitary thrift holding companies are able to affiliate with any company—financial or commercial. This narrow and well regulated universe does not pose the risks opponents to banking and commerce fear. A number of commercially-owned unitaries were formed in the late 1980s at the request of the Federal government as a small contribution to cleaning up the savings and loan crisis. Due to the massive failures in the savings and loan, the cost of the cleanup outpaced the government's ability to cover the insured deposits held by these failing institutions. Therefore, the government appropriately sought buyers, rather than absorb the cost of resolution. Many commercial firms acquired these thrifts and saved the Federal government untold billions. Now, Congress, without significant debate on the merits of this action, is reversing the rules these institutions operate under and is deleting a large segment of acquirers these institutions assumed when they purchased these institutions.

I feel that this action is wrong for two main reasons. The first is that the Federal government cannot continue to break its promises. All Americans should be concerned that if we break our promises to these "big bad businesses," who is next—veterans, seniors, the poor? Also, I fear that if we take this action, we are reducing our credibility the next time we have a crisis and ask the private sector to step in and assist. Although it seems easy to take this action today, I hope we do not regret it the next time we face a crisis.

ROD GRAMS.

ADDITIONAL VIEWS OF SENATORS SARBANES, DODD, KERRY, BRYAN, BOXER, MOSELEY-BRAUN, JOHNSON, AND REED

PRIVACY FOR CITIZENS' PERSONAL FINANCIAL INFORMATION

Although we are all supporters of H.R. 10, there is a significant issue that is not adequately addressed by this legislation: the protection of a customer's personal, confidential, financial information by a bank, securities broker-dealer, or insurance company.

Few Americans understand that, under current Federal law, a financial institution can sell, share, or publish customer transaction and experience data. Such data includes savings account balances, certificate of deposit maturity dates and balances, stock and mutual fund purchases and sales, life insurance payouts, and health insurance claims.

H.R. 10 would dramatically alter the U.S. financial landscape by allowing mergers that put under the roof of one holding company banks, securities firms, and insurance companies. Each affiliated institution will be able to offer its customers new products through "cross-marketing," or selling new products of affiliates to existing customers. Cross-marketing can entail sharing large amounts of highly sensitive, confidential customer information. Today's technology makes it easier, quicker, and less costly than ever before to have immediate access to large amounts of consumer information; to analyze data, to identify someone who, for example, is elderly or has a maturing CD; and to immediately send that data to others. Furthermore, this confidential information can easily be sold, shared or made public without the customer's consent or knowledge.

Both these new business affiliations and technology advances are fueling consumer concerns about the mishandling of personal information, and they have also highlighted the difficulties individuals face in trying to prevent inappropriate use. Selling and sharing this information will likely lead to increased telephone calls and mail solicitations.

A June 8, 1998 Business Week commentary entitled "Big Banker May Be Watching You" underscored the potential abuses:

> Suppose that when you retired, your bank started deluging you with mailings for senior services—each tailored to your exact income, health needs, and spending habits. Or your lender slashed your credit-card limit from $20,000 to $500 after you were diagnosed with a serious disease.
>
> Those two Orwellian scenarios may sound far-fetched, but they might not be for long. In the wake of the * * * mad rush by large insurers to acquire thrift charters, consumer advocates are raising valid questions about whether the insurance arms of these new conglomerates will share

sensitive medical records with their lending and marketing divisions.

Abuses arising from sharing information without a customer's knowledge or permission have already taken place. For example, the Securities and Exchange Commission (SEC) recently took enforcement action against a large national bank that had been giving sensitive customer financial information to an affiliated securities broker. The SEC found the bank employees and the securities affiliate employees "blurred the distinction between the bank and the broker dealer" and the affiliated broker's sales "representatives used materially false and misleading sales practices" which "culminated in unsuitable purchases by investors." The SEC also found many of the targeted bank customers were elderly and had never previously invested in securities: 65% were over 60 years old, 36% were over 70 years old; and 11% were over 80 years old. Many had low annual incomes: 47% were under $25,000 and 19% were $15,000 or less.

Other major corporations have bumped against privacy concerns while expanding their marketing services. In almost every case, the companies backed down only after the practices became publicly known and outraged consumers complained.

Additional abuses are easy to imagine:

—A bank could send names and account balances of elderly customers with maturing certificates of deposit that have large balances to an affiliated stockbroker who, in turn, could market riskier products to those customers.

—An insurer could send an affiliated stockbroker the names and the amount of payouts received by beneficiaries on the policies of recently deceased life insurance policyholders.

—A health insurer could send information on policyholders with claims for serious or terminal health conditions to an affiliated bank loan department.

—An entrepreneur could legally obtain this confidential information about a private citizen from a financial company and then set up a website that provides all of the financial and transactional information outlined above to anyone who wants to examine it.

The Committee has heard from many groups voicing support for consumer financial privacy protections. The American Association of Retired Persons (AARP) advocated that, "Consumers should be given the choice as to whether banks can share information about their accounts with any other entity." AARP is especially concerned about older Americans' vulnerability: "elderly Americans are among those most vulnerable to the complex and fundamental changes already occurring in this period of financial transformation—and they will be put at further risk by the financial mergers permitted by this proposed legislation if the issue of information privacy is not addressed."

Consumers Union has said, "As financial services firms diversify and 'cross market' an array of financial products, their interests in obtaining information about consumers is on a collision course with consumers' interest in protecting their privacy. * * * We believe legislation should prohibit depository institutions and their affiliates from sharing or disclosing information among affiliates or to third parties without first obtaining the customer's written consent."

The Free Congress Research and Education Foundation, Consumers Federation of America, Consumers Union, Electronic Privacy Information Center, Privacy International, Privacy Times, and U.S. Public Interest Research Group wrote on August 26, 1998 to all Senate Banking Committee Members to "sound an urgent alarm about the lack of protections for consumers' financial privacy." They complained, "Financial modernization will become a code phrase for 'privacy violation' unless changes are made to help ensure that consumer financial privacy is protected and that consumers have control over with whom information about them is shared or sold."

The letter elaborated on the problems we face:

> Current law would allow these companies to create a virtually unregulated centralized data base combining, for example, the health insurance, mortgage, stock brokerage and credit card data of their estimated 100 million customers, along with information from numerous outside data sources, ranging from credit reports and credit and insurance applications to public records and other information obtained from "data-mining" firms, without the informed knowledge or consent of their customers. * * * [H.R. 10] will create a whole new financial services landscape, putting consumers' personal, medical and financial information into a brave new world with greater privacy risks than ever before.

On September 9, 1998, The Washington Post published an editorial, "* * * And a Matter of Privacy," arguing,

> Along with medical records, financial and credit records probably rank among the kinds of personal data Americans most expect will be kept from prying eyes. As with medical data, though, the privacy of even highly sensitive financial data has been increasingly compromised by mergers, electronic data-swapping and the move to an economy in which the selling of other people's personal information is highly profitable—and legal.

The Post editorial concluded that the privacy amendment to H.R. 10, which was supported by all of the Democrats on the Committee, is "a protection well worth considering, especially in the banking context. As the pace of the much-touted 'information economy' quickens, safeguards against these previous unimagined forms of commerce become ever more important."

We firmly believe that a citizen should have the fundamental right to prevent his or her personal financial transaction or experience information from being sold or shared by a financial institution unless he or she has been given notice, has a chance to verify the accuracy of the information, and has agreed to disclosure.

During consideration of H.R. 10, we offered an amendment that would have protected the privacy of customers' financial information by directing the Federal Reserve Board, Office of Thrift Supervision, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and SEC to jointly promulgate rules requiring the institutions they regulate to: (1) inform their customers what information is to be disclosed, and when, to whom and for what purposes the information is to be disclosed; (2) allow customers to review the information for accuracy; and (3) for new customers, obtain the customers' consent to disclosure, and for existing customers, give the customers a reasonable opportunity to object to disclosure. These institutions could use confidential customer information from other entities only if the entities had given their customers similar protections.

Unfortunately, the Committee defeated this amendment by a vote of 8–10.

The majority argued simply that the issue was "too complex" to be dealt with in H.R. 10. At the same time, they admitted, "It is absolutely a problem that must be addressed." Also, it was acknowledged, "the industry should understand that this issue is not going to go away, and if they think they're just going to relax on it and nothing's going to happen, they're going to be making a big mistake."

We agree that the issue of protecting an individual's financial privacy is "complex." That is the very reason we proposed that the Federal financial regulators jointly promulgate rules on the subject and gave them 270 days to do so.

We also agree that the issue is "too important" and "is not going to go away."

The Financial Services Act of 1998 will provide unique and historic opportunities for banks, securities firms, and insurance companies. But bestowing these benefits upon these industries and allowing them to join together in a single holding company does not mean that consumers must surrender the confidentiality of their financial information.

In fact, the United States already faces pressure from the European Union as a result of our inadequate privacy protections. The European Union Data Protection Directive, which goes into effect October 25, 1998, goes much further than any privacy protections in place in the U.S. or even contemplated by the Administration. The Directive mandates that member states protect privacy rights in the data collection by both the public and private sectors. It prohibits the transfer of data without first obtaining the individual's unambiguous consent regarding the transfer and use of his or her personal financial data. The Directive provides "that the transfer to a third country of personal data * * * may take place only if * * * the third country in question ensures an adequate level of protection." Since indications are that the European Union views current U.S. privacy policy as inadequate, U.S. businesses are likely to have difficulties marketing to European consumers.

Moreover, it is our view that industry self-regulation, which has been tried during the past few decades, is not working. The Privacy Protection Study Commission, established by the Privacy Act of 1974, recommended privacy legislation in a number of fields, including banking, credit, and insurance. The recommendations applied the key privacy principles of notice, consent, and verification of information. In 1996, after two decades of surveys and academic studies which showed little progress implementing privacy rights, the former Chairman of the Privacy Commission wrote: "The [1977] commission, at the behest of industry, recommended that companies be allowed to follow its guidelines voluntarily. But 19 years later, it is clear that Congress should turn the commission's suggestions into law."

Recent studies by the FTC and the FDIC have also found self-regulation to be ineffective. The FTC June 1998 report, Privacy Online: A Report to Congress, observed: "To date, the Commission has not seen an effective self-regulatory system emerge." The FDIC August 1998 Financial Institution Letter, Online Privacy of Consumer Personal Information, reported: "The FDIC conducted its own informal survey of Web sites of FDIC-supervised banks. The FDIC's survey findings were comparable to the FTC's."

We believe that the protection of the privacy of customers' personal financial information is much too important to ignore any longer. It should be addressed in H.R. 10.

BASIC BANKING

We regret that the Committee failed to retain the important lifeline basic banking provision included in the House-passed version of H.R. 10. The provision was designed to ensure that low-income individuals will have access to basic banking services within the new financial holding company structure. The provision would have required that as a condition of a bank holding company becoming a financial holding company, all subsidiary insured depository institutions of the bank holding company must offer and maintain low-cost basic banking accounts.

The provision addressed a significant problem: banking services are beyond the reach of millions of Americans. According to a recent study by the U.S. Public Interest Research Group, the average cost of a checking account is $264 per year. The cost represents a major obstacle to establishing a relationship with a bank for families at or near the poverty line. Conservative estimates by the Comptroller of the Currency place the number of households without a basic banking account at 12 million.

Because they cannot afford banking services, many Americans are shut out of the economic mainstream. This lack of access compels many low-income individuals to become customers of fringe bankers and pay high costs to access the payment system. For instance, they utilize the services of high priced check-cashing businesses and money order services. In addition, some individuals are forced to operate on a cash-only basis which places them at risk for their personal safety. Further, many individuals find it difficult to establish traditional credit without a banking account.

We also agree with the rationale of the House-passed provision, that it is imperative that low-income individuals have access to basic banking services in light of passage of the welfare reform law and the Electronic Benefits Transfer Act. These laws mandate that all Federal government transfer payments be made electronically.

The Committee heard from many consumer groups, including the Consumer Federation of America, Center for Community Change, and the National Community Reinvestment Coalition, that supported the inclusion of this provision in H.R. 10. During House

Banking Committee hearings, NationsBank and BancOne expressed support for the basic banking provision.

We disagree with arguments that a basic banking requirement would be burdensome and unworkable. Many large banks currently offer basic banking accounts on a voluntary basis. Moreover, seven states currently have statutes requiring some form of lifeline banking. The experiences of these states indicate that a meaningful and useful basic banking requirement is possible on the Federal level.

In our view, the requirement that a bank offer low-cost basic banking accounts if it wants to exercise the expanded powers permitted by H.R. 10 is a very modest one with large public benefits. We hope that it can be restored during the course of the legislative process.

PAUL SARBANES.
CHRISTOPHER DODD.
JOHN KERRY.
RICHARD BRYAN.
BARBARA BOXER.
CAROL MOSELEY-BRAUN.
TIM JOHNSON.
JACK REED.

ADDITIONAL VIEWS OF SENATOR REED

The Senate Banking Committee's passage of H.R. 10 represents a significant step forward in Congress' efforts to modernize the Depression-era laws governing our financial services industry. I voted in favor of the bill because I believe that institutional and technological changes which have taken place in the financial services industry have cast doubt on the need to maintain the existing separation between banking, securities, and insurance activities. Indeed, these barriers between financial activities have made it increasingly difficult for U.S. financial firms to realize economies of scale and compete with their international counterparts. Notwithstanding my support for the bill, however, there are several issues that I believe should be addressed as the Senate contemplates further action on the bill.

At the behest of the Federal Reserve, H.R. 10 would require financial services companies to conduct activities through affiliates that are subject to Federal Reserve regulation. Historically, national banks have been able to conduct many of these activities through an operating subsidiary of the bank. As a result, H.R. 10 limits the flexibility of financial services firms in conducting activities. This limitation, I believe, runs counter to the goals of modernization embodied in H.R. 10.

The effect of the organizational structure established in H.R. 10 is to give the Federal Reserve, an independent and politically unaccountable agency, the unbridled discretion to regulate financial services firms. In so doing, the bill limits the authority of the Treasury Department and the Office of the Comptroller of the Currency to regulate the activities of national banks, a function in which these agencies have been engaged since 1864. As a result, I am concerned that the Federal Reserve, whose primary occupation is monetary policy, will be less responsive to public concerns and may not vigorously exercise its regulatory authority over financial institutions.

Inherent in H.R. 10 is the consolidation of banking, securities, and insurance activities in one business enterprise. To regulate these activities, H.R. 10 has adopted a functional approach which places banking regulation under the appropriate bank regulator, securities regulation under the Securities and Exchange Commission and insurance regulation under the relevant state. The Federal Reserve acts as the "umbrella" regulator over these functional regulators. This new structure has not been effectively tested in practice, particularly under the excruciating pressure of the failure of a large financial institution. Because of this dispersion of regulatory authority, a significant financial failure could produce regulatory stalemate rather than an effectively coordinated response.

Central to Congressional consideration of financial modernization legislation must be the protection of the taxpayer-backed deposit insurance funds. Following the savings and loan crisis of the 1980s, in which taxpayers paid $60 billion to cover depositor losses from failed thrifts, Congress must be careful not to create opportunities for abuse that could lead to a future crisis.

While there are a number of prudent safeguards included in H.R. 10, the bill, by its very nature, will allow the creation of financial behemoths, which, in a time of crisis, could bankrupt deposit insurance funds and require a taxpayer bailout. Conventional wisdom is that because of the size and importance of such institutions to the economy, they would be too-big-to-fail, and the government—i.e. taxpayers—would be obligated to bail out the institutions.

Unfortunately, H.R. 10 does not address the potential inadequacy of deposit insurance funds to recapitalize a troubled mega-bank. Moreover, H.R. 10 does not address the "too-big-to-fail" problem. As we go forward, I believe these issues should be considered and addressed.

Finally, I am concerned that H.R. 10 does not do enough to promote affordability and access to retail banking services such as checking accounts. Provisions in the House-passed bill requiring banks to provide low-cost, basic banking accounts were, unfortunately, stripped out in the Senate Banking Committee. This is of great concern in light of recent evidence suggesting that large institutions, of the type that will be created under H.R. 10, generally charge higher fees for retail banking services. As a result, I fear that the cost of banking services for many Americans may increase.

Moreover, by failing to include low-cost banking provisions in H.R. 10, Congress is foregoing a tremendous opportunity to provide access to the banking system for the 10 million Americans who are currently "unbanked". In my view, financial modernization by its very terms must provide the broadest possible access to the banking system, thereby promoting savings and investment activity, which stimulates economic growth. H.R. 10 ought to help the unbanked become banked.

I voted to favorably report H.R. 10 out of the Senate Banking Committee. I did so because I believe the bill goes a long way in eliminating unnecessary and outdated laws which have hampered the competitiveness of the U.S. financial services industry. Nevertheless, I believe the concerns that I have raised should be addressed if we are to produce balanced legislation that will provide a sturdy regulatory framework that will encourage economic expansion and ensure the safety and soundness of our financial industry.

JACK REED.

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